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# WEST BANK AND GAZA UPDATE

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# Doing More

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## Editorial: Doing More

In the previous editorial of September 2006, the World Bank stressed with pride our continuous presence in, and support to, the West Bank and Gaza since 1993. Over this period, the Bank has used over US\$510 million of its resources to finance projects in the Palestinian Territories. These projects have created hundreds of employment opportunities, supported over 3,500 infrastructure projects, constructed 1,700 classrooms, rehabilitated or constructed 600 medical facilities, built over 750 kilometers of water and sewage lines, rehabilitated 1,300 kilometers of roads, and during the intifada helped 700,000 children to attend school and assisted 220,000 children to graduate from high school.

However, the challenge for us has been and continues to be to do more, not only in helping deliver economic and social services to the Palestinian people, but in supporting viable institutions that will propel Palestinian development and self-sufficiency.

During his recent visit to the Palestinian Territories, Mr. Juan José Daboub, World Bank Managing Director, fulfilled our commitment to do more by signing three new project agreements worth US\$25 million. These projects are: the Emergency Municipal Services Rehabilitation Project II; the Palestinian NGO Project III; and Additional Financing for the Bank's existing Integrated Community Development Project.

These projects seek to support access to basic social and economic services in poor and marginalized communities in the West Bank and Gaza, including solid waste collection, street lighting, wastewater and electricity services, health services. They will also provide temporary job opportunities to unemployed Palestinians, and help sustain reliable mechanisms for delivery of emergency social services. At the same time, the projects are structured in such a way so as to build the capacity of local communities through job creation, and initiatives that will provide the basis for long term sustainability of these services.

These three new projects now raise the number of active World Bank programs to eleven, consisting of approximately US\$117 million in World Bank grants. In addition to this, our Managing Director also announced during his visit the decision of the World Bank's Board of Directors to extend an additional US\$50 million grant for future projects to assist the Palestinian people.

The way ahead is a critical one, where the World Bank and other institutions must continue to do their utmost to ensure that the Palestinian people do not suffer through periods of uncertainty and conflict. More importantly, we must keep our eyes on the prize- the goal of building permanent and sustainable Palestinian structures to provide services to the people, and to manage a much needed economic development program. Such a program will only succeed if it is built on clear and transparent governance, the free movement and access of people and goods, and an open economy able to trade with all its neighbors and the world.



# The Role and Performance of Palestinian NGOs

## In Health, Education and Agriculture

World Bank  
Bisan Center for Research & Development  
English full report: "[www.worldbank.org/ps](http://www.worldbank.org/ps)"

The World Bank's recent study investigates the role and performance of Palestinian NGOs (PNGOs) as service providers in three sectors – health, education and agriculture. It provides systematic information on the work of PNGOs, identifies areas of strength and weakness and suggests how their contribution to service delivery and the socio-economic development process might be improved.

The work on this study was initiated in late 2004/early 2005, a time when Palestinians were facing a number of difficult challenges, including a faltering peace process and political instability, a deeply depressed economy, reduced levels of per capita income and great financial scarcity. Dependency on donor funding had also escalated making Palestinians the recipients of one of the highest levels of per-capita Official Development Assistance (ODA). Nevertheless, the period was also characterized by a degree of hope associated with the Israel's impending 'disengagement' from Gaza and parts of the West Bank (WB), and the prospect of enhanced levels of donor and private investor contributions to a process of economic reconstruction. In this context the Palestinian Authority (PA) was leading the consultative preparation of a Medium Term Development Plan (MTDP).

Today, following Hamas' victory in the PLC elections of January 2006 and the international response to this, the political and economic outlook is far worse, at least in the short term. Nevertheless, the findings of the study remain relevant since they provide insights into the constraints

and opportunities that PNGOs will face under almost any imaginable scenario. At a time of near paralysis of the PA's service delivery systems, assumptions about the extent to which NGOs can replace the PA abound, and the results of this study will hopefully moderate unrealistic expectations. The study also aims to offer NGOs the opportunity to reflect on their achievements and constraints, and to assess how they can best adapt to changing circumstances. Finally, the study offers guidance to the PA and donors on how they might aim to develop more systematic approaches to supporting service delivery.

The study data was for the most part gathered through two surveys: i) an NGO Survey, encompassing 78 independently registered PNGOs and a selected number of their service delivery facilities; and ii) a Household Survey covering 3000 households. The findings from the NGO Survey should be treated as indicative, given the relatively limited size of the sample. The surveyed parameters include

The review of the role and performance of PNGOs is focused on an analysis of their delivery function which specifically looks at: (a) patterns of utilization; (b) accountability and management practices; (c) targeting and participation practices; and (d) quality standards and their monitoring. The study also reviews the constraints faced by PNGOs in accessing donor funding, as well as their level of cooperation with the PA and other local partners.

# Main Findings

## The Role of PNGOs Relative to Other Service Providers

*The study shows that the role of PNGO vis-à-vis other service providers varies considerably across and within the three sectors reviewed. The demand for NGO services is, as one would expect, influenced by the availability and relative cost of alternative channels of service delivery. PNGO services are most frequently used when the PA has a limited role or weak capacity, and where the cost of acquiring services from the private sector is high. The scale of PNGO service provision is largest in agriculture, followed by vocational training and pre-school education; it is less significant in the health sector. Within sectors, however, PNGOs seem to deliver specific services that are otherwise unavailable or inaccessible, and have thereby developed specific niches of specialization.*

In the health sector, according to data from the Ministry of Health (MoH) and the Palestinian Central Bureau for Statistics (PCBS), PNGOs account for 29% and 32% of the total number of primary health care centers and hospital beds respectively, and for 26% of the human resources employed by the sector.<sup>1</sup> PNGOs also reportedly account for up to 20% of donor funding in this sector. But at the same time, and according to the results of this survey, PNGOs only account for 11.7% of the total household utilization of health services. The MoH, UNRWA and private providers, respectively, account for 46%, 24% and 16% of the total.<sup>2</sup> In Gaza, where UNRWA accounts for up to 46% of health service utilization, the share of PNGOs drops to as little as 8% of the total. However, a much higher rate of utilization of NGO services is reported for specialized services, including rehabilitation, psychological counseling and health awareness and training where NGOs account for 19%, 25% and 21% of services utilized, respectively.

The low utilization of NGO health services is explained by the availability of public health insurance and (in UNRWA's case) free services. The PNGOs' high share of facilities, staff and resources spent in the sector, though suggest considerable inefficiencies in resource allocation.

In *education*, where the role of the Ministry of Education and Higher Education (MOEHE) is focused on formal basic and secondary education, PNGOs account for 21% of pre-school services and the private sector another 71%. In vocational training, the private sector and PNGOs each account for 25% of total services, and the PA 37%.

In *agriculture*, PNGOs account for up about 53% of services, compared with the PA's 30% and the private sector's 18%. The limited role of the PA in agricultural services is consistent with a sector policy that stresses PA regulation rather than service provision.

## The Beneficiaries of PNGO Services

*The study shows that services offered by PNGOs are not equally accessible to the poor in the three sectors. PNGOs have to charge a fee for the services they deliver, and therefore when they have the option of receiving the same service, but for a lower price, the poor will generally not choose to utilize PNGO services. Therefore, the study confirms that in many instances, the beneficiaries of PNGO services are largely from households with higher income levels. However, as mentioned, the profile of PNGO beneficiaries varies considerably across the sectors reviewed.*

In the *health* sector, poor households with incomes below NIS 1,400/month<sup>3</sup> amount to 40% of the beneficiaries of PNGO services---but to 60% and 65% of the beneficiaries of public and UNRWA health services respectively. PNGO health service beneficiaries are divided equally between urban and rural inhabitants. Utilization of PNGO health services, however, seems to be consistent across urban and rural areas.

Household participation in *pre-school education* is slightly correlated with income levels: the rate of participation was lowest (at 20%) amongst families with income levels below NIS 750/month, but increased to 28% amongst those reporting an income of more than NIS 2000/month. PNGOs provide almost a quarter of pre-school education in rural areas, but only some 13% in urban centers. 50% of families using PNGO pre-school services came from families with incomes below NIS 1400/month, as did 47% of those accessing private sector providers.

Overall, households belonging to the income bracket of less than NIS 1400/month accounted for 50% and 60% respectively of all beneficiaries of *vocational training* and *agricultural services*---and of PNGO services in these

1 See MOH/Health Management Information System (HMIS) for PHC and Hospital bed data (2004), and PCBS Survey for Human Resources data (2005).

2 It should be noted that according to the 2004 data of the Ministry of Planning's Aid Coordination Department, 20% of total ODA to the West Bank and Gaza is channeled through PNGOs.

3 Using a poverty line income of US\$2.1 per day, an average family of 6 needs to be earning NIS 1,700 per month to be "over the poverty line".



sectors as well. The participation of women in vocational training programs offered by NGOs was notably higher than in the case of Government and private sector providers.

In terms of targeting policies, only in the agricultural sector did PNGOs confirm that they targeted their services to marginalized areas or poor households (43% of respondents, as opposed to 10% in health and 11% in education). However, all PNGOs identified individual income level as an important criterion for beneficiary selection. Furthermore, PNGO targeting of vulnerable groups, e.g. the disabled, youth, children/women, was frequently reported.

### NGO Accountability

*By and large, PNGOs appeared to be more concerned with 'vertical accountability' to their boards of directors, to the PA and to donors than with 'horizontal accountability' to their broader constituencies and the communities they served.* The reported rate of dissemination and disclosure of annual and financial reports to General Assembly members, local community groups and partners was very limited. The reported regularity of Board meetings and the range of responsibilities held at that level suggested that PNGO Boards are actively engaged in governing and overseeing the work of their organizations. There seemed to be some ambiguity, however, about who in the PNGO hierarchies approved financial reports and the selection of auditors, raising some concern about the adequacy of PNGO financial control and oversight.

On the other hand, the study evidenced a fairly rigorous level of monitoring and reporting on grant-financed projects—albeit at the behest of donors. PNGO capacity to investigate the broader impact of their services outside specific project frameworks was generally much less developed, with the level of participation by beneficiaries in the design and assessment of service delivery programs also very low.

### Leadership and Management Practices

*While PNGOs are led by highly professional staff, selection processes used for recruiting PNGO directors are generally non-competitive and lack transparency—reinforcing the perception that PNGOs are governed by a 'small elite'.* Furthermore, and despite recent reporting on further PNGO decentralization, authority on key matters continues to be very centralized amongst the majority of PNGOs surveyed. This is somewhat offset by the flexibility that local branches and facilities appear to enjoy in introducing new lines of service delivery, which enhances PNGOs' responsiveness to local needs. It was also noted that the staff of PNGOs are in general afforded few opportunities for training and skills development.

### Quality of Service Delivery

*The study confirmed that PNGO's monitoring of quality and impact was weak largely on account of the absence harmonized quality standards.* Thus, while NGOs had adequate operating procedures for tracking patient health status and student achievement, or following up on

referrals, only the larger ones monitored impact according to clearly identified benchmarks. When asked about the results/impact of their work, PNGOs were generally much better able to report on processes and outputs rather than outcomes. The monitoring of service standards by PA specialized agencies was also noted to be weak.

*The overall rate of beneficiary satisfaction with PNGO services was very high, a judgment largely based on the perceived competence and professionalism of PNGO staff and the quality of PNGO resources and facilities, in particular in health.* This positive overall assessment varied by sector, though. In the vocational training sector, beneficiaries were more satisfied with services provided by PA and private sector providers, with 25% of the beneficiaries of PA programs reporting that the training had helped them to find a job, compared to only 14% amongst those trained under PNGO programs.

Similarly, although the beneficiaries of PNGO agricultural services rated them in general more positively than those provided by the Government, this was not so in relation to starting new activities or increasing their income levels. This is likely explained by the fact that the PA and the private sector facilitate/provide credit and access to markets, while PNGOs concentrate more on the provision of training, subsidized agricultural inputs and land reclamation.

## Funding Patterns

*The study confirmed that the capacity of PNGOs to generate local revenues is limited to the larger organizations, in particular to hospitals and NGOs working at the national level.* Service fees and income generating projects account for the largest share of revenues generated by these organizations. Islamist NGOs also reported high levels of local community contributions, an avenue not yet fully explored by other surveyed organizations.

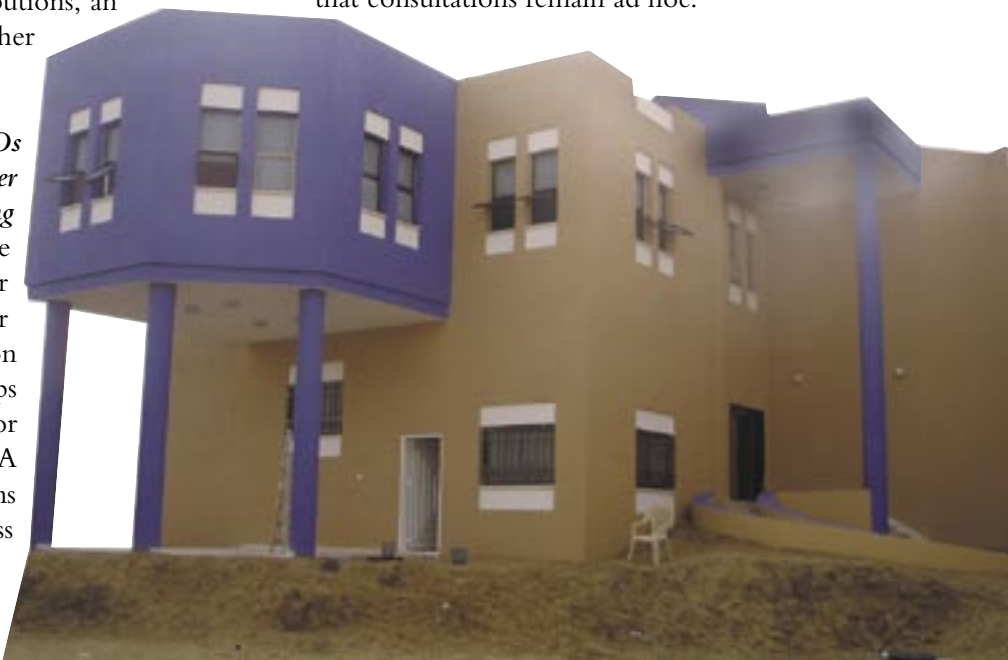
*International funding for PNGOs is reported as biased towards larger PNGOs, and to those working in the health sector.* This can be explained in part by the greater institutional capacity that larger NGOs tend to possess, in addition to long-established relationships with international NGOs and donor organizations. Funding from the PA and from other local sources seems to be more evenly distributed across

PNGOs of varying sizes. This may in part be attributed to the fact that smaller PNGOs receive financial support from the Ministry of Labor and Social Affairs (MoLSA), and are also sub-contracted by PA institutions to deliver specific services to marginalized communities.

*The study confirms that the work of PNGOs is heavily constrained by the unpredictability and lack of transparency in the provision of donor funding.* Donor grant funding and reporting policies are generally perceived as overly complex, and funding is seen as provided in general for excessively short periods of time, a factor which hinders the ability of PNGOs to plan ahead and to focus on improving quality and sustainability.

## Cooperation with the PA and other Local Partners

*The study confirms that there is considerable cooperation between PNGOs and the PA, with the role of the PA generally perceived as positive.* However, cooperation between the two does not extend to the level of partnership or active collaboration in policy and sector planning. This could be explained by a combination of the limited capacity of the PA to lead sector planning processes as well as a lack of coordination amongst PNGOs in pursuit of a systematic dialogue with the PA. The study also reveals limited involvement on the part of those NGOs surveyed in advocacy work aimed at influencing PA sector policies. Furthermore, amongst those who reported having an advocacy role, their focus was on meetings, the distribution of educational materials and coalition building, as opposed to meetings with PLC members or preparing policy documents. More recently, however, the PA (in particular the Ministry of Planning) was seen as more interested in consulting with PNGOs (for example, in the context of the preparation of the MTDP). At the level of line ministries, the evidence is that consultations remain ad hoc.



*Cooperation between PNGOs, local government and the private sector remains very limited.* This could be attributed to the lack of legitimacy that local governments have enjoyed until the recent municipal elections, and the inability of local government to provide an enabling environment for community development. Lack of cooperation with the private sector also points to untapped potential to promote corporate contributions to PNGO programs and activities.

## Conclusions

In summary, the surveys indicate that

- The level of beneficiary satisfaction with PNGO services is high, and in many cases higher than for comparable PA services.
- The relationship between PNGOs and the PA is generally constructive, albeit with limited involvement by PNGOs in sector policy and planning. In contrast, PNGO partnerships with local authorities are weak.
- PNGOs have carved out niches in areas and/or sectors where PA service provision is not available or is limited, and where private sector fees are relatively steep.
- PNGOs are not as a matter of course reaching out to poor and the marginalized communities. That said, most NGOs make efforts to give priority to poor and disadvantaged individuals in the groups they have elected to work with. The fact that PNGOs need to charge fees for their services goes some way to explaining the lack of systematic focus on the poor.
- Donors tend to favor the larger PNGOs, due in large part to their capacity to comply with complex donor procedural requirements; donors also tend to fund for relatively short periods, which is inconsistent with the creation of long-term capacity and, ultimately, PNGO sustainability
- PNGOs are not in most cases accountable to beneficiaries and local communities, but rather to their own boards, donors and the PA. This lack of “horizontal” accountability can be correlated with limited beneficiary involvement at all stages of the service process.

- From an institutional perspective, PNGOs have some way to go in terms of objective monitoring and impact evaluation, as well as internal management and staff development. NGO senior executives are customarily recruited without open competition.

## Recommendations

The following recommendations arise from the study’s analysis:

- The Palestinian population is increasing rapidly; the economy, beset by conflict and closure, is currently unable to sustain adequate levels of public welfare (let alone improve them). In such a context the need for PNGOs as service providers is likely to increase with time, and donors should recognize this through appropriately enhanced levels of support. To improve the effectiveness of PNGO support, though, donors need to develop a better awareness of capacity and demand within the entire service delivery system.
- The PA and PNGOs should collaborate on developing simple, transparent quality and performance standards for service delivery. In parallel, efforts to strengthen the monitoring function of the specialized ministries should be intensified.
- PNGOs should be supported and encouraged to target their services more explicitly towards the poor. Given the particularly high rates of poverty in Gaza, PNGOs should be encouraged to expand their presence there, complementing the role of the PA and UNRWA.





- Given their important role as representatives of civil society, PNGOs should broaden their constituency base with both civil society and grassroots based organizations. This process should be accompanied by increased advocacy of more equitable and inclusive social policies.
- PNGO networks and umbrella organizations should intensify efforts to enhance accountability through the development and adoption of a PNGO Code of Conduct (which should include measures designed to increase transparency in hiring, policy formulation and financial management). For its part, the PA can assist the development of the PNGO sector by activating the PNGO Law's By-Laws which were approved by the Cabinet and which clarify ambiguities in the existing Law. This would help promote greater transparency and improved performance in the sector.
- Opportunities for forming PNGO partnerships, in particular with local government, should be more actively explored---possibly through joint funding mechanisms. Such partnerships are very important to the long-term sustainability of PNGOs.
- Donors should take a more systematic approach to PNGO funding, placing less emphasis on ad hoc project financing and more on sub-sectoral programs. Donors should also be prepared to support PNGO activities on a more sustained basis in order to allow for fuller institutional maturation to take place. Donors should also place more emphasis on supporting the professional evolution of PNGOs. This should help develop PNGO transparency, and thereby legitimacy vis-à-vis the public and beneficiaries. The PA and donors could also consider NGO representation in their aid-coordination structures to help create greater harmonization with donor-financed developmental/institutional building programs delivered through the PA.

# Public Expenditure Review From Crisis to Greater Fiscal Independence

Full Report: [www.worldbank.org/ps](http://www.worldbank.org/ps)

The Palestinian Authority (PA) is confronting a fiscal crisis that could threaten its very existence. During the first six months of the Hamas-led government, tax revenues amounted to \$17 million per month, compared to \$104 million during the same period the year before. Expenditures for the same period in 2005 stood at \$172 million per month; by 2006, they had fallen by more than half. By December 2005, the wage bill alone was running at around \$93 million per month. The proximate causes are Israel's withholding of clearance revenues and U.S. regulations against banks engaged in financial transactions with the PA. The structural roots of the crisis run deeper. By late 2005, the PA position was already fiscally unsustainable, with assets being liquidated or mortgaged to meet current expenditure needs.

The current crisis provides an opportunity to take a longer term and more strategic view of Palestinian finances. Throughout 2005, the PA was running an average monthly deficit in excess of \$60 million, nearly 60 percent above the average monthly revenues it was receiving. With unchanged policies, the fiscal deficit for 2006 would in all probability have exceeded \$900 million and perhaps gone over \$1 billion. This is almost three times the amount secured in external budget support in 2005.

The dynamics behind the PA's increasingly precarious financial position—and the failure to curb the rapid expansion in the wage bill—have been understood for a decade or more. More than seven years ago, civil service employment stood at 48,000, and staffing in the security services at 41,000. As of 2006, these figures stood at over 81,000 for the civil service and 77,000 for the security services. Even in the midst of acute financial crisis in the first quarter of 2006, the PA has added 1,300 into the civil service and 6,800 into the security services.

Employment in the public sector is driven by a host of complex dynamics. Some are understandable, such as the relatively high levels of unemployment and demographic pressure to create jobs for new entrants into the labor force; the collapse in remittances from workers in Israel; a highly constrained private sector's inability to absorb surplus labor; and the pressure to incorporate irregular militia into the security forces in Gaza. Others are less so, such as the use of employment within the PA for political patronage. Certain donor approaches have also contributed to the fiscal situation and, in some cases, contributed to the erosion of reforms in areas such as public financial management.

Placing the PA back upon a sustainable fiscal trajectory will require coordinated effort on the part of all relevant parties around a shared strategic approach. It will also require a significant change in PA financial and administrative practices.

## Macro and Fiscal Challenges

Beset by closures, violence and a fiscal crisis, the Palestinian economy is declining from its already low level. In the short term, continued donor assistance would be critical for sustaining the Palestinian economy. A solid foundation for future growth depends on two factors: a radical improvement in Palestinian movement and access, and stabilization of the PA's fiscal situation. This would require both resumption in the transfer of clearance revenue and significant fiscal adjustment on the part of the PA.

The Government of Israel's decision to suspend the transfer of clearance revenue, which accounts for over 60 percent of the PA's revenues, has made it virtually impossible to achieve sustainable fiscal management. However, the PA's past spending policies have exacerbated the current crisis. Despite a revenue crunch during the *intifada*, the PA's wage bill continued to increase by 11% per annum between 1999 and 2005. Moreover, since 2003 the PA has increasingly been the "financier of last resort" to cover unmet obligations for other public entities. In 2005, such payments drained the public resource envelope by \$344 million, or more than 5 percent of GDP. New social benefit programs were launched and pension laws adopted which have also increased the PA's burden. The increase in the deficit was mostly covered through domestic financing (including the Palestine Investment Fund and bank loans), but this source of financing has reached its limits.

## Public Financial Management

From 2000 to 2004, the PA implemented several public financial management (PFM) reforms that have significantly improved transparency. These include setting up a Central Treasury Account (CTA); formulating an annual budget that is approved by the Palestinian Legislative Council (PLC); creating an accounting system for orderly budget appropriations and execution; placing Ministry of Finance (MOF) financial controllers in every line ministry; transferring payroll responsibilities to the MOF and paying public sector salaries through bank accounts; establishing the Palestine Investment Fund (PIF); and enhancing fiscal transparency by posting the Budget Speech and expenditure reports on the MOF's website.

Unfortunately, these reforms are now at risk. By 2005, momentum for PFM reforms was slowing, and a number of initiatives—particularly those involving financial reporting and internal audit—were experiencing delays. More importantly, the CTA has been a casualty of the recent political standoff between donors and the Hamas government.

## Civil Service Reform

The civil service reform agenda is one of the most important challenges confronting the PA. Any near-term effort should involve a comprehensive payroll audit, the use of biometric systems; the development of human resource information systems capable of sharing information between the MOF, General Personnel Council (GPC) and Ministry of Interior (MOI); consolidation of security service payrolls under the MOF; and clarifying the roles of the GPC and the MOF under the new civil service legislation.

Other important reforms include strengthening the institutions and legal framework for combating corruption. The PA must develop an anticorruption strategy that focuses on prosecution, prevention and public awareness, as well as conduct empirical work on the nature and causes of corruption. The general inefficiency of the court system hampers investigations of cases of corrupt practices in the civil service. In the medium term, strengthening of the court system and the office of the attorney general should be a priority.

## Intergovernmental Fiscal Relations and Municipalities

Palestine has one of the more vibrant local government sectors in the region. Municipalities and villages within the West Bank & Gaza are among the most autonomous. Central government transfers are modest by regional standards, and local governments have a great deal of control over their own revenues.

Yet the second *intifada* has heralded the problem of spiraling municipal financial arrears, heavy reliance on utility service surcharges for revenues, and a larger share of local expenditures for administration and wages. Over the past few years, capital expenditures have declined. This raises important questions about service delivery and coverage, and whether municipalities will be able to maintain and expand infrastructure services. There is a need to consolidate the legal framework, to ensure greater coordination among national and local agencies, to rationalize the rising number of local governments, and to review the incentive frameworks such as the use of pre-paid metering to prevent municipalities from defaulting on their utility payments.

## Health and Education

The health and education systems have seen significant accomplishments over the years. The expansion and equitable access achieved in the education sector is comparable with most middle-income countries. Enrolment in basic education is universal, and the enrolment rate for secondary education is above 80%. In 2004, the infant mortality rate was 22 deaths per 1,000 live births, well below the regional average of 44. Total life expectancy at birth was 73 years, on average 4 years longer than the typical person in the MENA region. The under 5 mortality rate of 24 deaths per 1,000 under 5, it is less than half of the regional average of 56.

However, there is scope for savings across these sectors. Shifting demographic trends imply the need to recruit fewer teachers in the future. Savings can also be realized by changing the mix of staff. A comparison with UNRWA, for example, reveals that the PA employs over twice as many support personnel. The PA's practice of procuring new textbooks annually results in unnecessary spending. Most importantly, the PA can reorient its expenditure from recruiting more teachers and building more schools to developing pedagogical methods, improving the quality of teacher training, and enhancing capacity to monitor performance.

In health, total spending (including direct household spending) is about 13% of GDP, among the highest in the region. PA expenditure on health services has been driven by increasing public employment, with almost no funding for capital expenditures and a diminishing share for operating costs. The PA's expansive wage bill and expenditure for contracted services with NGOs has left little fiscal space for pharmaceuticals, medical supplies and operations and maintenance.

## Social Services

Despite current financial difficulties, the PA providers of social services have pressed on with their tasks. Some social programs are still operating, albeit in a limited form. Food rations from the World Food Program (WFP) continue to be distributed, the UNRWA Social Hardship Case program and other services are functioning, and food rations for newly poor families in Gaza are being issued. The Ministry of Social Affairs is currently working with the World Bank to improve the targeting of benefits.

Yet reforms are needed in this sector, particularly with the pensions schemes that are among the most generous in the world—more generous than those in donor countries

who are being asked to fund the program. A step would be to strengthen the capacity of the GPIC (Gaza Pension Investment Corporation), and to review the Unified Pension Law to ensure long term sustainability. Similar reform is needed for the 2003 Social Security Law for private sector workers. And the 2005 pension law for security services is simply unaffordable.

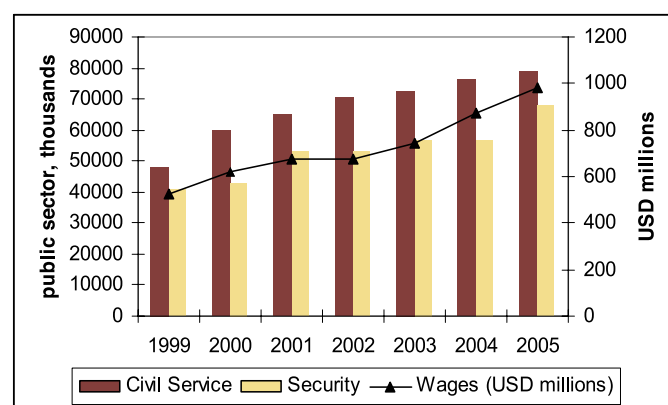
## Towards a Sustainable Wage Bill

Since March 2006, the government has been unable to pay most of its salary commitments owed to PA employees. The totals vary between categories of employees, but on average employees have received around 40% of their normal incomes. Around 71% of government employees fall below the poverty line defined as income level of less than \$460 per month for an average household of six as compared to 35 percent in June 2005.<sup>1</sup>

While it is impossible for the PA to cover its costs under current circumstances, analysis reveals that the wage bill was already unsustainable before the current fiscal crisis (Figure 1). No realistic amount of donor funding or increase in tax and clearance revenues could be expected to bridge the gap.

A sustainable plan would involve a comprehensive payroll audit, followed by the termination of all ghost workers, double dippers and staff serving past retirement. The PA can also restrict overtime payments to only those working in front-line service delivery in the Ministry of Health.

Figure 1- Public Sector Hiring and Wage Bill Growth, 1999-2005



Source: World Bank Staff Calculations, 2006

1 Source: Near East Consulting Monthly Bulletin on Palestinian Perceptions Towards Political, Economic, and Social Conditions, Bulletin No. 11, November 8, 2006.

These measures should be combined with improvements in control (particularly placing the MoF in charge of security service payroll) and a hiring freeze for the next two years. If the wage containment plan goes well, the hiring freeze could be relaxed to allow replacement recruitment for front line staff in the Ministries of Health and Education.

Beyond these steps, the PA could pursue options for long-term wage sustainability, including to roll-back the 2005 salary increases in some form. Bank calculations indicate that this could save the PA around \$317 million annually over the first two years and a net present value of \$1.2 billion over five years. Since public sector wage rates are now around 15% greater than those in the private sector, the justification for this is strong.

A second approach would be to offer voluntary retirement packages to civil and security servants. The design and composition of such programs could vary, and preliminary calculations indicate that potential savings could be in the range of \$417 to \$718 million over a five year period. A third approach would involve a wage bill cap allocated over a fixed number of employees according to an agreed formula. A target could be \$80 million per month—approximately the level prior to the major salary increases in July 2005. This sum would represent a savings of roughly \$240 million per year. Should the PA make progress in retiring staff and/or reducing the number of employees, higher salaries would be paid to the remaining employees.

Moving forward, the key is to revise the incentive system between the PA and donor community. Current donor practices have subsidized both wage and non-wage spending, allowing the PA to shift resources away from non-wage expenditures towards salaries. Donor efforts to contain the wage bill through vehicles such as the Public Financial Management Reform Trust Fund made the mistake of linking specific wage bill targets to a percentage of revenue, which allowed the PA to expand recruitment as revenues went up.

The challenge of reducing the wage expenditures for the security services will be particularly difficult. First steps would include a transparent accounting of their numbers; a reduction of the “non-compliant” officers recently identified by the MoI; and other measures. Many officers are nearing or past retirement age and could also be

induced to leave. Such efforts would need to be carefully developed and coordinated with ongoing efforts to reduce the number of security services from 13 to 3. The chances of success of security sector reform (SSR) are greater if such a strategy is part of a comprehensive political framework that includes reconciliation, the rebuilding of institutions, support to disarmament, demobilization and reintegration, and measures to improve the rule of law. SSR and demobilization operations need to be timed carefully in order to complement each other and support the overall peace process.

## Conclusion

For a decade or more, the PA has been able to avoid hard choices with regard to its public employment policies. While the temptation is to view overstaffing as a long-term problem to be tackled once the private sector is able to absorb the additional labor, the reality is that the status quo is not tenable. One way or the other, salary rationing will take place. The question is whether it will take place in a coherent and equitable fashion leading towards a desirable medium-term goal, or in a series of uncoordinated, ad-hoc adjustments punctuated by weak performance, unfulfilled expectations, employee hardship and labor unrest.

Sadly, lost within this broader story are some important successes by the PA in public financial management, municipal governance, education, health and the social services. Even in civil service reform, the PA has passed a law applying stricter recruitment rules and measures for non-compliance, has strengthened the role of the General Personnel Council (GPC), and has improved MOF control over the payroll.

All of this progress is at risk unless the PA, the donor community and the Government of Israel can come up with a collective plan for restoring PA finances. For the PA to be viable, it needs to receive the clearance revenues it is entitled to from Israel under the 1994 Paris Protocol of Economic Relations. The Central Treasury Account must be re-established and the practice of routing aid flows through the Office of the President shut down. Arab donors need to continue their high levels of support, and mechanisms such as the Economic and Governance Strategy Groups need to play an important role in coordinating donor assistance.

# World Bank Investment Climate Assessment

## Findings and Recommendations

# F

## indings

Recently the World Bank has undertaken an Investment Climate Assessment (ICA) for the West Bank and Gaza (WBG). An ICA is a standard World Bank study that has been completed in many countries around the world. Its purpose is to link the business environment, or what is termed the Investment Climate, directly to firm level performance and make specific policy recommendations to help the private sector. The ICA is based on all available information but is underpinned by an enterprise survey conducted in face to face interviews of more than 400 enterprises throughout WBG by the Palestine Central Bureau of Statistics. Since it is a standard survey it allows for a comparison between the investment climate in WBG and other countries.

The ICA reveals that shrinking market access and the lack of free movement are the main constraints to growth for Palestinian enterprises. Relative to other countries the Palestinian investment climate is good: petty corruption is low, the bureaucracy is relatively efficient and financial markets are well developed. Despite this, Palestinian firms have not invested enough to maintain their international competitiveness. Managers know they need to invest and have access to the necessary resources. However, they are unwilling to do so unless they are assured secure and predictable access to both domestic and international markets.

Palestinian industry developed to produce low value, labor intensive goods for highly protected local and Israeli markets. However, as Israel has moved toward higher value goods and opened its markets to free trade, Palestinian producers have suffered. Most Palestinian enterprises are no longer internationally competitive in the low value goods they specialize in. Enterprises are

very small – average size is five workers – and average capacity utilization for manufacturing enterprises is only about 50 percent. Few firms invest. Most machinery is over 10 years old, less than 26 percent of the surveyed enterprises did any worker training and only a small share had international quality standards. In addition, since the WBG economies are tied to Israel, they have a higher cost structure than other countries producing labor intensive products. Industry's share of GDP in WBG has fallen to less than 15 percent. If it is going to grow and provide jobs for the rapidly expanding population, Palestinian entrepreneurs will have to invest and move to high value goods that can compensate for the high costs of production. They will also have to look beyond the Israel and develop new markets in other parts of the world.

In recent years the Palestinian Authority (PA) has attempted to provide the investment climate to support the needed investment. The financial sector is highly liquid and less than 15 percent of the survey sample is financially constrained. Most enterprises do not have a bank loan. But that is because they don't want one given the few profitable investment opportunities and not because the banks will not lend to them or the required collateral is too high. Corruption and government regulations do not appear to be a major constraint to investment. Most managers reported not having to pay any bribes and for those who did, they paid less than in other countries. The average time it took to obtain a business license was only 30 days, which is half the time reported in Turkey. Senior managers in Palestine also reported spending on average less than 7 percent of their time dealing with government regulations, compared to over 8 and 12 percent in Turkey and Lebanon respectively. The Palestinian Authority is new and just beginning to develop its institutions but they appear to be emerging in an efficient manner.

# P

## olicy Recommendations

Unfortunately, the movement restrictions imposed by the Israeli authorities, which prevent Palestinian firms from accessing markets and create high levels of uncertainty, overshadow other elements of the investment climate. The percentage of West Bank and Gaza enterprises selling into the other territory has fallen by half since 2000. More importantly, markets in the West Bank appear to be shrinking because of movement restrictions imposed to protect Israeli settlements. In 2000 nearly 60 percent of firms made a significant share of their sales outside of their home city; by 2005 this had fallen to around 40 percent. The most difficult issue to overcome is the uncertainty caused by the movement restrictions. For example, the survey reveals that on average it takes around 22 days to clear imports for companies in the West Bank. But the longest time averages nearly 43 days. On time delivery is a requirement in the modern export market, but Palestinian producers can never be sure when their cargo will move. Consequently, to a large degree, they are frozen out of the high value export market.

The ICA identifies three major areas that need to be addressed to help the Palestinian private sector: restore movement and access, develop private enterprise capabilities and continue to measure and improve the investment climate.

Without free internal movement and dependable access to the world market there can be no viable Palestinian economy. Major issues include restoring free movement within the West Bank, including the Jordan valley; resuming trade between West Bank and Gaza; opening the Rafah crossing to movement of goods and restoring access to East Jerusalem and the Israeli market for Palestinian producers. It is also necessary to improve the access for Palestinian goods to the rest of the world through Jordan.

Palestinian firms have very few sources of enterprise learning and find it hard to find and adopt new technologies required to increase productivity and move up the value chain. They have been cutoff from the export market, they receive no foreign direct investment and have little access to international consultants. Any policies or programs that assist individual Palestinian enterprises in finding new technologies or reduce the considerable risk of investing in the current conditions will benefit the economy as a whole.

Finally, the investment climate must be constantly measured and improved. Before the recent turmoil, the PA was making progress in creating a strong enabling environment. But the work was far from finished, and there remains much to be done to create institutions that will allow business to prosper. The land registration system, courts, Palestinian Standards Institute, Customs and a host of other agencies all need to continue to develop to enable the private sector.



# Olive

and the Olive Oil  
Sector in Palestinian  
Territories



## How important are olives to the Palestinian economy?

Today, there are approximately 900,000 dunums planted with 10 million olive trees, constituting 45 percent of cultivated land in Palestine and contributing as much as 15 – 19 percent of agriculture output.<sup>1</sup> Moreover, there are about 100,000 families depend on olive harvest for their livelihoods. In 2006, olive oil production is estimated to reach 33,000 – 35,000 tons; of which around 12,000 tons are estimated to be consumed locally and the rest will be available for export or storage.

## What are the main privileges of the Palestinian olive oil?

First, The Palestinian climate and soil enable the production of some of the highest quality olive oil in the world. To illustrate, the unique taste and aroma of Palestinian olive oil has been recognized in taste tests conducted by certified testers in Europe. Second is the unintentional low use of chemical fertilizers, herbicides, or pesticides that have allowed many Palestinian producers to enter the high value organic market. According to a 1998 survey by the Palestinian Central Bureau of Statistics, about 21 percent of the total area under cultivation received chemical fertilization and less than 15 percent used pesticides or fungicides. Moreover, the Palestinian olive oil has unique marketing options. It can be branded as oil from the “holy land”, and in some Arab and ethnic markets it will draw support to assist Palestinian labor.

## How time is significant during harvesting and pressing?

To produce the best oil, olives must be harvested at the correct time and moved to the presses as quickly as possible. Delays in harvesting or in moving harvested olives to the presses reduce the yield and quality of oil produced.

Palestinian farmers in the West Bank now face over 500 physical obstacles and closures restricting their movement;



a 40 percent increase since 2005. Farmers are often prevented from accessing their trees making it difficult to prune the trees, plow and control weeds, which reduces yields. To produce the necessary high quality olive oil, Palestinian farmers should be granted access to their fields and presses, and kept safe from settler attacks. Unlike previous years, the Israeli army and ministry of defense made some effort to ensure farmers’ access to their lands to pick olives.

## What are the main challenges that are facing the Palestinian olive oil industry?

Palestinian olive oil industry faces tremendous challenges that can be divided to two main categories: technical and logistical. First, many trees are found on steep terraced hillsides which necessitate farmers to carry on plowing, weed control, harvesting, and other activities manually or by using animals. This in turn contributes to the high cost of picking which amounts to \$1.5 per kg of olive oil. There are other technical problems facing this industry including, but not limited to, lack of manual machineries for plowing, picking, and harvesting, lack of ventilated boxes and stainless steel storage facilities, as well as *Thubabet Al-Zaytoun* (olive fly) that negatively affects both the quality and quantity of the harvest.

Second, the limited access to water supplies is hindering the ability of many farmers to provide partial irrigation when the fruits are blossoming and the rains have stopped early. The full access to water supplies and the removal of any Israeli restrictions from digging new wells or developing new irrigation projects is vital in terms of substantially increasing yields.

<sup>1</sup> Agriculture accounts for nearly 25 percent of GDP.

## What are the main challenges that restrain Palestinian producers from entering the export market?

The export market is primarily constrained by the relatively high cost of production resulting from a combination of factors including nature of the terrain, movement restrictions, as well as the cost structure inherited from the Israeli economy. First, many trees are found on steep terraced hillsides which necessitate farmers to carry on plowing, weed control, harvesting, and other activities manually or by using animals. As a result and despite the use of unpaid family labor, labor accounts for over half of the total cost of olive oil production.

Second, the movement restrictions raise transport costs and prevent Palestinian exporters from committing to specific delivery schedules. According to one Palestinian exporter, the cost of moving a 20-foot container to the port has doubled since the beginning of the most recent Intifada, and internal transportation constitutes approximately 20 percent of total shipping cost. Besides, Palestinian producers have to pay a \$200 per container security fee that Israeli shippers do not face. Moreover, creating predictability for Palestinian producers is the most critical aspect. Their inability to plan shipments and commit to specific delivery dates, Palestinian producers will be unable to substantially expand exports.

Third, the Palestinian economy is essentially a part of the Israeli economy and has a similar cost structure. Consequently, production costs are higher than in neighboring countries or in major producing countries. Informal estimates suggest that production costs in the West Bank are 20–30 percent higher than in Jordan, 10–15 percent higher than Syria, and 35–40 percent above the cost in Turkey.

Finally yet importantly, entering the world market requires Palestinian producers to develop the necessary contacts and marketing skills. As in all aspects of the industry, the closures have an adverse effect on marketing. It is difficult and expensive for Palestinian entrepreneurs to travel abroad to make market contacts. Foreign buyers often will not enter the Palestinian territories and Palestinians are often not allowed into Jerusalem to meet them. Sending samples, attending trade fairs, and the other basic acts of establishing presences in new markets are all much harder and more expensive for Palestinians.

## What can Palestinian producers do to be competitive in the export market?

To compensate for the high costs of production and to increase the value added from olive oil, producers will have to capitalize on the superior quality and special marketing niche of Palestinian oil and move toward the high end, extra virgin or organic bottled market. Palestinian producers must establish a “made in Palestine” brand name with a reputation for quality that compensates for its higher price. To do this, producers will have to significantly increase quality, raise productivity, and lower costs. Local producers estimate that small bottles earn 15–20 percent more than bulk exports and organic oil can earn as much as 40 percent more.

Producing high quality oil that is suitable for the export market requires large investments to build storage facilities, modern presses, and to teach farmers proper harvesting methods. Yet, if producers are unsure that they will be able to access external markets they will be unwilling to make the investment, and will continue the low risk strategy of producing low quality bulk oil. Hence, Israel must protect its security while also ensuring that legitimate businesspersons can easily travel and export without unnecessary delays.

Furthermore, most of the current production is classified as ordinary virgin due to the lack demand of local market for high quality oil. In addition to targeting farmers and producers, raising consumers’ awareness is critical in improving quality. With some effort and support at different levels, it is possible to produce large quantities of extra virgin oil in the West Bank.

Finally, the support of the Palestinian Authority and organizations like Palestinian Olive Oil Council is essential in terms of creating and monitoring standards and providing agriculture extension services for the farmers.

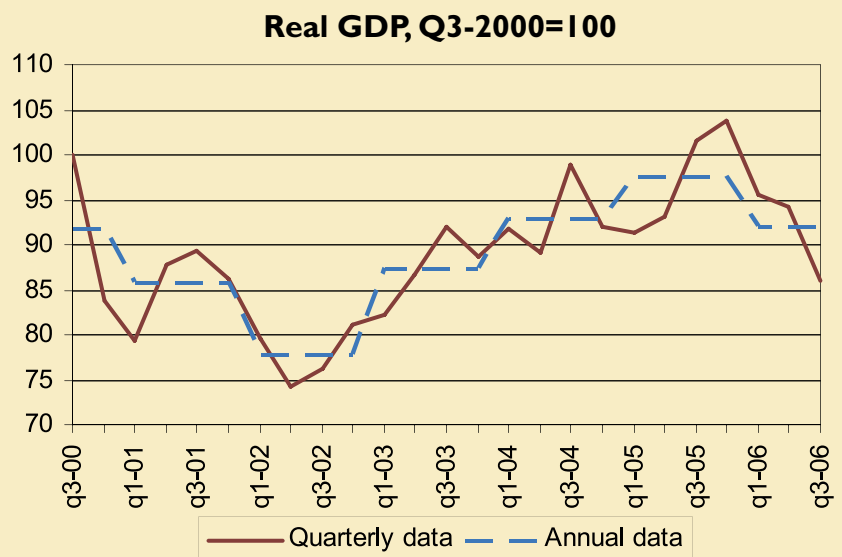


# Overview of Recent Economic Developments<sup>1</sup>

Prepared jointly by the World Bank and IMF

## Economic activity

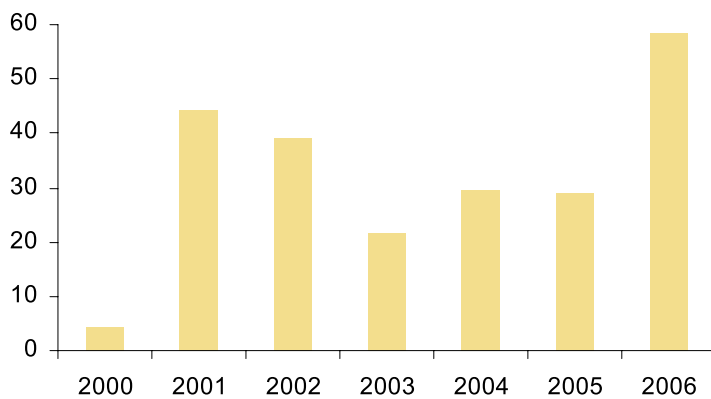
The Palestinian economy is once again declining. Quarterly GDP data recently released by the Palestinian Central Bureau of Statistics show that GDP (in real terms) declined steadily during the first three quarters of 2006<sup>2</sup>. Calculated as an average over the year, the decline is equal to 5-6 percent—adding population growth of 3-4 percent, the decline in per capita GDP amount to 8-10 percent. This is a sharp reversal of economic trends the past three years, in which the Palestinian economy recovered from its precipitous decline during the first three years of the *intifada*. A decline of this magnitude would leave GDP per capita around US\$1,000 and real GDP per capita some 32 percent lower than in 1999.



<sup>1</sup> A more detailed description of fiscal and financial developments from April to September 2006 can be found in "West Bank and Gaza: Recent Fiscal and Financial Developments", October 2006, [www.imf.org/wbg](http://www.imf.org/wbg).

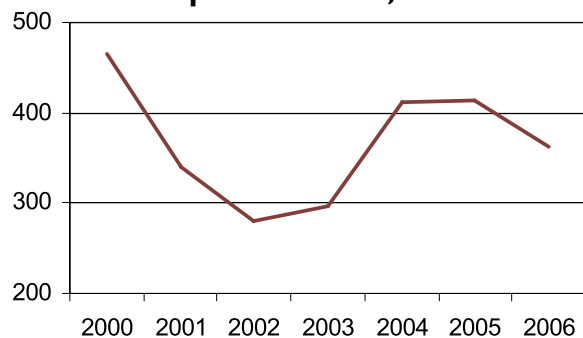
<sup>2</sup> The Quarterly National Accounts data is only preliminary, and may be revised later. Due to the difficulties on the ground, the quality of the underlying data is deteriorating. PCBS estimates of indirect taxes—which determine the difference between GDP at factor costs and GDP at market prices—is subject to particularly uncertainties as the clearance revenue is not being transferred.

**Budget support, US\$ mill./month**



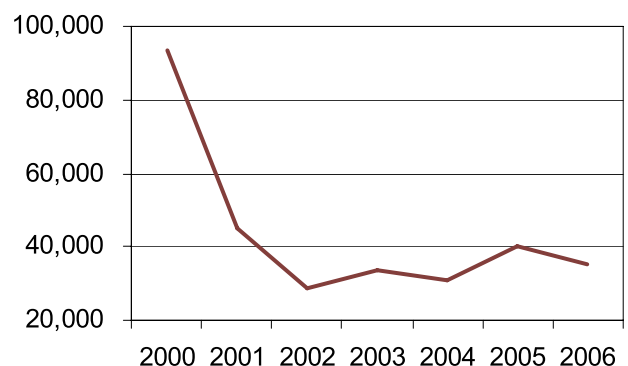
Stepped-up donor support has played a major role in sustaining the economy and household incomes. Following the inauguration of the Hamas' government in March 2006, donors terminated or were unable to provide direct financial flows to the PA government. At the same time, however, donors significantly increased the flow of rapid-disbursing assistance flowing to the West Bank and Gaza, through channels outside of the government. The IMF estimates that a total of more than US\$700 million have been provided in what can be considered equivalent to budget support during 2006, compared to US\$349 million during 2005. This has been an exceptionally high level of assistance, provided to help cover the PA's recurrent budget expenditures. Data for other donor support (emergency/humanitarian assistance, mainly through UNRWA and NGOs and development aid) are notoriously difficult to measure. However, indications are that disbursements of emergency/humanitarian assistance have increased in 2006<sup>3</sup>, while disbursements of development aid have declined. The Bank estimates that US\$100 million in additional donor support increase Palestinian GDP by 2-3 percent – the increase in budget support alone could thus have prevented a further fall in GDP of c. 8-10 percent.

**Export to Israel, USD**



Closures remain tight, to the detriment of Palestinian export. Movement restrictions and border closures continue to stifle the normal conduct of commercial activities. In interviews for the Bank's forthcoming WB&G Investment Climate Assessment more than 60 percent of Palestinian businesses reported instability and transportation issues are the most important impediments to Palestinian private sector activity. The Bank's ongoing monitoring of Palestinian movement and access shows that the number of trucks carrying exports from Gaza have dropped 40 percent from the already low level at the beginning of 2005, and remain far from the targets set in the November 15, 2005 *Agreement on Movement and Access*. In their monthly business survey, the Palestinian Central Bureau of Statistics reports that conditions continue to worsen for business owners. For the most part, over 2005 (when economic growth was relatively strong), perceptions leaned toward the positive, with, on average, only 10% of firms indicating on a month to month basis that conditions had deteriorated. Over 2006, however, that proportion had more than tripled to 34%. Palestinian export to Israel, the main market for Palestinian exporters, declined by 15 percent in nominal terms during the first half of 2006 compared to the previous 6-months period<sup>4</sup>.

**Workers in Israel**



Movement restrictions reduced the number of Palestinians working in Israel. An average of 35,000 Palestinians worked in Israel and Israeli settlements during the first six months of 2006, compared to 40,000 in the year 2005 – equivalent to a decline of 12 percent<sup>5</sup>. The decline was especially large for workers without permit, indicating increasing difficulties for clandestine workers to circumvent

3 For example, as of September 30, 2006, the UN's Refugee and Works Agency (UNRWA) had received pledges worth US\$129 million against their emergency appeal; an increase of 15 percent compared to the pledges for the full year in 2005.

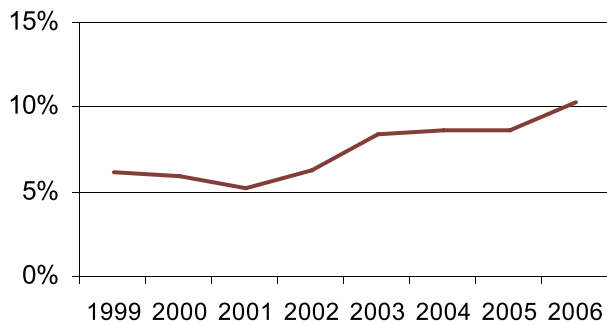
4 While this is a large decline, and an indication of a further tightening of the closure regime, it should be noted that it is still smaller than assumed in the March 15 "Worst Case" Scenario.

5 The number exclude an estimated 24,000 Palestinians residing East Jerusalem who can unhindered work in Israel.

Israeli checkpoints and other restrictions, including the Separation Barrier. The number of Palestinian workers with permit declined 7 percent. Virtually no Palestinians from Gaza work in Israel anymore.

Employment declined in Gaza, but continued to rise in the West Bank. During the first nine months of 2006 the number of jobs in Gaza declined 11.2 percent compared to the same period a year before. Between Q3-2005 and Q3-2006 almost 20,000 jobs were lost in Gaza. At 166,924, the number of jobs in Gaza has fallen close to its level 6 years ago, at the eve of the *intifada*. The unemployment rate (ILO definition) in Gaza reached 36.3 percent. By contrast, in the West Bank, employment levels during the first 9 months of 2006 have increased moderately compared to the same period a year ago, partly as a result of increased employment in the service sector, although the manufacturing and transport sectors have also registered higher employment. The unemployment rate in the West Bank was 19.1 percent in Q3-2006.

#### Share of under-employed in total employment



Increased scarcity of jobs has led to more part-time workers. Also indicative of the increasing scarcity of jobs is that the share of workers reporting that they work less than full time has increased steadily the past year. In Q3-2006 the share reached 11.6 percent, up from 7.3 percent of Q4-2004<sup>6</sup>. Employment data for the fourth quarter of 2006 is scheduled to be released in February 2007. A continuation of the current situation would likely result in further job-losses being reported by then, although the olive-harvest reportedly was exceptionally good this year, and would be expected to have led to some temporary job creation.

The economic outlook is highly precarious. In the short term, continued high levels of donor assistance would be critical for sustaining the Palestinian economy. A solid foundation for future growth, however, would depend on two factors: First, a radical improvement in Palestinian movement and access; under the current set of restrictive measures the Palestinian economy will remain moribund.

Second, a stabilization of the PA's fiscal situation, which would require resumption of the transfer of clearance revenue, and a significant fiscal adjustment by the PA.

## Fiscal developments

Resources to fund recurrent government expenditures remained severely constrained in the last quarter of 2006. External support was relatively strong, but was not enough to offset the drop in tax revenues—largely because Israel continued to withhold indirect taxes (so-called clearance revenues) it collects on behalf of the PA—and banks being a drain on resources, instead of a source of financing, as they continued to reduce their exposure to the government.<sup>7</sup> In the last quarter, about \$136 million in external support had been disbursed by mid-December, of which some \$104 million was channeled through the Temporary International Mechanism (TIM) and \$32 million received from Arab donors via the accounts of the Presidency. This brought the total amount of external support received in 2006 to over \$700 million. All three windows of the TIM are now fully operational. The scope of its allowances has been expanded and now reaches over 140,000 beneficiaries. Together with the Arab donors, the TIM has been instrumental in cushioning the adverse impact of the diplomatic and financial isolation of the government on the Palestinian population.

The limited financial resources available in the last quarter of 2006 were used largely for payments to government employees and social hardship cases, and, to a lesser extent, to ensure the continued supply of fuel and utilities. By mid-December, an additional \$110 million in payments to government employees had been made, which meant that, since the Hamas-led government took office at end-March, they received on average some 40 percent of their normal incomes, but with considerable differences in this ratio between various categories of employees.

The disintegration of the public financial management system continued. Sizable amounts of cash were reportedly brought in from abroad in 2006, without adequate recording of the amounts or their uses. More generally, reporting on fiscal operations has weakened further.

<sup>6</sup> The number of hours worked by those reporting being “under-employed” is not known. Assuming that they work half-time, the increase in the share of under-employed has resulted in a 2.2 percent decline in the total number man-hours.

<sup>7</sup> For comparison, total resources available to finance recurrent government expenditures in the last quarter of 2005, including tax revenues, external support, and domestic financing, amounted to almost \$525 million.

Fiscal developments obviously depend heavily on the political situation. Despite the recent agreement on a Unity Government (the Mecca Accord), the political outlook continues to be uncertain. There is thus a continued prospect that the political impasse witnessed during 2006 will continue, both domestically and internationally, for at least several more months. Consequently, financial resources—and thus spending—can be expected to remain severely constrained. Even assuming continued

strong Arab support of \$40–50 million per month, sizable TIM disbursements of some \$30–40 million per month now that it is fully operational, and \$15 million per month in domestic revenues, this would still cover only about half to at most two-thirds of monthly recurrent expenditures, and less if banks continue to reduce their exposure to the government. In this case, fiscal policy will remain limited to carefully selecting which payments to make using available funds.

## Financial sector developments

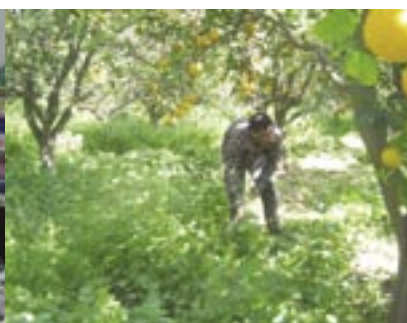
The Palestine Monetary Authority (PMA) has been actively addressing the fall-out of the political difficulties on the financial sector. So far, the situation has been manageable and banks in West Bank and Gaza (WBG) remain liquid. Deposits have continued to grow—non-government deposits increased by almost 6 percent in the twelve months to November 2006—apparently reflecting strong inflows from abroad. Banks have also continued to extend credit to the private sector, although this has slowed considerably in recent months; credit to the private sector increased by 7 percent in the twelve months to November. Banks do have a sizable exposure to the Palestinian Authority (PA) and to PA employees. They have been able to significantly reduce their exposure to the PA, while a large part of the remaining loans to the PA are collateralized by the assets of the Palestine Investment Fund. Debt service obligations due by PA employees have been relatively small, in part because loans were rescheduled. Banks have also started to deduct small amounts from allowances and partial wage payments paid to government employees to help cover interest due. But as loans to PA employees have little or no collateral, other than wages and personal guarantees, these loans will become a concern if normal payments of PA salaries do not resume in the near future. In this case, banks will need to start provisioning for them. Loans to PA employees are spread across several banks, but the risks are mainly concentrated in a few domestic banks that have a narrower capital base. The PMA is working with these banks to develop remedial plans aimed at reducing the size of loans to PA employees relative to their capital, including by retaining all profits.

Also, the PMA has been working closely with the Bank of Israel (BoI) to ensure continued relations between Israeli banks and those in WBG. Measures agreed with the BoI focus mostly on improved disclosure by both sides on bank transactions, in line with international practice, and prohibiting check endorsements. The new Anti-Money Laundering/Combating Financing of Terrorism (AML/CFT) implementing regulations adopted recently in Israel—which include tougher identification and reporting requirements for transactions with banks in WBG and which are to be implemented within one year—together with similar regulations issued in October by the PMA to banks in WBG—which are to be implemented within six months—should enable banks on both sides to continue doing business with each other.

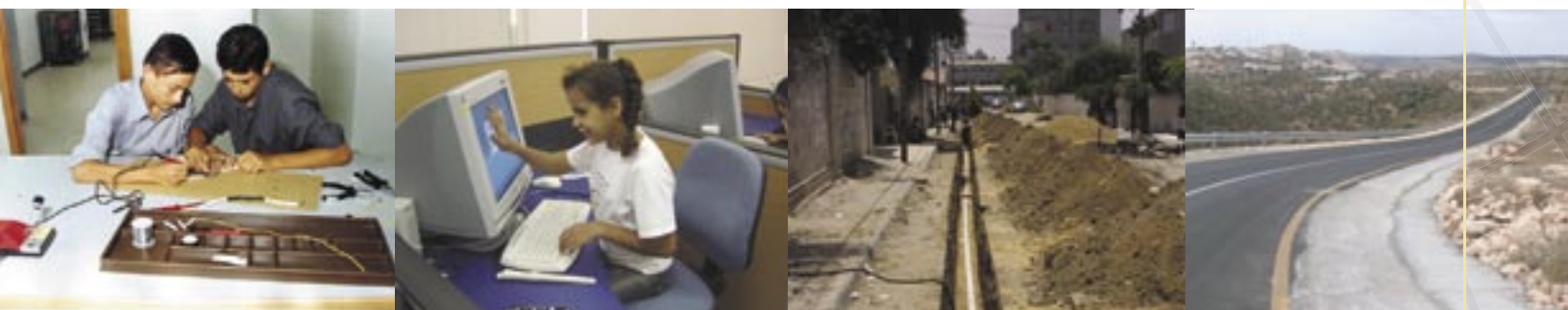


# The World Bank's Operations in West Bank and Gaza

On-going Bank Group Operations	
Project Name & Details	Description
<b><i>Solid Waste and Environmental Management Project (SWEMP).</i></b> World Bank: US\$9.5 million Approval Date: October 10, 2000. Closing Date: December 31, 2007. Task Team Leader: Andrew Mokakha	The Project is financing interventions in solid waste collection, transfer, and disposal of waste for the District of Jenin. The Project is managed by the Joint Services Council for Solid Waste Management (JSU). The Project is assisting in strengthening capacity building of the Environmental Quality Authority. The EC is financing the supply of collection vehicles and transfer stations relation set-ups.
<b><i>Electric Sector Investment and Management Project (ESIMP).</i></b> World Bank: US\$15 million. EIB: US\$38 million. Italy: US\$35 million. PA: US\$3 million. Approval Date: August 31, 1999. Closing Date: December 31, 2006. Task Team Leader: Somin Mukherji	The objectives of this US\$91 million Project are to rehabilitate the power distribution systems in the central and southern West Bank, and to address the institutional structure for longer-term sector management.
<b><i>Emergency Water Project (EWP).</i></b> World Bank: US\$12.5 million Approval Date: February 2004 Closing Date: June 30, 2007 Task Team Leader: Sana Al Nimer	The main objective of the project is to support investments that would help alleviate the chronic shortages of safe water supplies; reduce water costs and health risks; and conserve scarce water resources by reducing system losses. The Project includes the following components: (a) emergency water supply repair and rehabilitation in remote rural areas of the southern West Bank; (b) repair and rehabilitation necessary to maintain water and sanitation service levels in the Gaza Strip at the high levels achieved under the Gaza Water and Sanitation Project despite the deteriorating economic and security conditions; and (c) Technical Assistance and Capacity Building provided to the Palestinian Water Authority and the recently established Coastal Municipal Water Utility in the Gaza Strip and to form pilot joint services councils for smaller towns in the southern West Bank.
<b><i>Social Safety Net Reform Project (SSNRP).</i></b> World Bank: US\$10.0 million Approval Date: July 19, 2004 Closing Date: December 31, 2008 Task Team Leader: David Steel	The objectives of the Project are to mitigate the impact of the present social and economic crisis on the most vulnerable, and to protect the human capital of poor children in the West Bank and Gaza. This objective is achieved through enhancing and modifying the existing Special Hardship Case (SHC) program of MOSA to include a component that will make eligible households' receipt of assistance conditional upon their compliance with a set of pre-determined criteria related to school attendance, attendance at scheduled health check-ups, and attendance at awareness session on pertinent social issues. The Project also aims to strengthen the institutional capacity of PA agencies involved in the implementation of the proposed project, in particular in Ministry of Social Affairs.



<p><b><i>The Integrated Community Development Project (ICDP).</i></b>  World Bank: US\$10 million plus US\$5 million supplemental financing approved in December 2006..  Approval Date: May 23, 2002.  Closing Date: December 31, 2006.  Task Team Leader: Husam Abu Dagga</p>	<p>The Project seeks to improve the quality and availability of basic social and economic services in poor and marginalized communities of West Bank and Gaza. It succeeds previous community development operations financed through the Bank under Community Development Projects I &amp; II. The project finances the rehabilitation of roads, water supply and sanitation systems, schools, clinics, thereby preserving and extending the capital stock of villages and small municipalities. It also finances agricultural activities, including the rehabilitation of wells, roads, and terraces. Lastly, the project is piloting new Information and Communication Technology (ICT) initiatives by funding the creation of Multipurpose Tele-centers, thereby improving access to information and training for the poor and marginalized.</p>
<p><b><i>North Gaza Emergency Sewage Treatment Project.</i></b>  World Bank: US\$7.5 million  Approval Date: September 9, 2004  Closing Date: June 30, 2010  Task Team Leader: Sana Al Nimer.</p>	<p>The North Gaza Emergency Sewage Treatment project is the fourth in a series of Bank-funded water and sanitation projects since 1994. The Project is addressing the immediate and impending health, environmental and safety hazards to the communities near the poorly-treated and rapidly growing sewage lake in the Beit Lahia area of North Gaza. The project is also part of a long-term solution for the adequate treatment and disposal of wastewater in North Gaza, which entails the construction of a new wastewater treatment plant expected to be financed by various donors. Approximately 300,000 people living in North Gaza will benefit from this project.</p>
<p><b><i>Gaza Water and Sanitation Services Project (GWSSP II).</i></b>  World Bank: US\$25 million  Approval Date: June 7, 2005  Closing Date: January 31, 2009  Task Team Leader: Khairy Al-Jamal</p>	<p>This Project is a follow-up to the previous GWSSP. The development objectives of this Project are: (a) to develop a sustainable institutional structure of the water and wastewater sector in Gaza by supporting the functional establishment of a Coastal Municipalities Water Utility, as well as by enhancing and deepening the involvement of the private sector through an eight-year operating contract and strengthening the regulatory and institutional capacity of the Palestinian Water Authority; and (b) to continue improving the water and sanitation services by rehabilitation, upgrading and expansion of existing systems and facilities. Like the GWSSP, this Project is part of a larger parallel capital program to improve water and sanitation services in Gaza. The Project includes substantial investments in the establishment of a bulk water supply network connecting the various municipalities in Gaza, in the sewerage network, and in wastewater treatment plants. These investments, totaling about US\$340 million for 2000-2005, will be financed by soft loans and grants from EIB, USAID, and KfW.</p>



<p><b><i>Tertiary Education Project</i></b>  World Bank: US\$10 million  Approval Date: April 26, 2005  Closing Date: December 31, 2009  Task Team Leader: Adriana Jaramillo</p>	<p>The project development objectives are: 1) to improve the regulatory environment for tertiary education management, relevance and quality assurance; 2) increase internal and external efficiency of the tertiary education system, as a first step towards seeking sustainability; and 3) to create incentives and provide the basis for improvements in efficiency, quality and relevance of tertiary education institutions in order to meet the socioeconomic needs of the Palestinian population. The project provides technical assistance on defining policies consistent with increasing the financial sustainability of the sector and improving the capacity to respond to labor market needs. It also provides incentive mechanisms to improve quality and relevance of the programs offered. On a competitive basis, institutions will apply for quality and management grants, administered by a Fund mechanism. In addition the project will provide technical assistance to improve the management of the current student loans program managed by the MOEHE, and will set the basis for expansion of the financial resources available for funding the student aid programs. The EC is providing co-financing in the amount of € 6 million.</p>
<p><b><i>Land Administration Project</i></b>  World Bank: US\$3 million  Approval Date: January 26, 2005  Closing Date: December 31, 2007  Task Team Leader: Ibrahim Dajani</p>	<p>The objective of this project is to assess/learn the extent of commitment and readiness of the PA to reforming land administration by introducing policy, legal and institutional changes to achieve efficient procedures for the issuance of land titles and registration of property transactions, and transparent processes for the management and disposal of public land. The project is the first phase of a long-term Land Administration Program, which aims at enhancing economic growth by improving land tenure security and facilitating the development of efficient land and property markets in rural and urban areas through the development of an efficient system of land titling and registration based on clear, transparent and coherent policies and laws and supported by an appropriate institutional structure.</p>
<p><b><i>Third NGO Project</i></b>  World Bank: US\$10 million  AFD: €6 million  Approval Date: December 19, 2006  Task Team Leader: Meskerem Brhane</p>	<p>The objective of the project is to provide social services to those who are poor, vulnerable or affected by the deteriorating socioeconomic conditions by establishing an effective mechanism to improve the quality and sustainability of NGO social service delivery. The project has also been designed to contribute towards institutional development of the NGO sector and contribute to equity in access to social services for the poor and marginalized.</p>

<p><b><i>Second Emergency Municipal Services and Rehabilitation Project</i></b>  World Bank: US\$10 million  Approval Date: December 19, 2006  Task Team Leader: Steve Karam</p>	<p>A prolonged period of economic contraction has had serious consequences for municipal revenues and the ability of local governments to continue providing basic services. This has translated into sharply increased health and sanitation risks for the Palestinian population resulting from mounting solid waste, and deteriorating streets, water and wastewater networks, particularly in heavily populated urban areas. The objectives of EMSRP II are to (a) provide funding for infrastructure rehabilitation and maintenance to help mitigate further deterioration in the delivery of essential municipal services, and (b) create temporary job opportunities at the local level through the launching of labor-intensive employment generation schemes. In addition, through the Municipal Development Lending Fund (MDLF), the Project would pilot innovative initiatives to improve municipal service cost recovery (through the introduction of pre-paid electric metering systems) and leverage partnerships with local NGOs to deliver services more effectively. The total cost of the project is currently estimated at US\$40.2 million with financing of US\$10 million from the Trust Fund for Gaza and West Bank (TFGWB), and further commitments from Netherlands and Agence Française de Développement. On-going discussions with KFW and Sweden are likely to cover the balance with commitments expected by March 2007.</p>
<p><b><i>Avian Influenza Prevention and Control Project</i></b>  World Bank: US\$10 million  Global Fund for Avian Influenza: US\$3 million  Approval Date: September 7, 2006  Task Team Leader: Husam Abu Dagga</p>	<p>West Bank and Gaza has been considered at high risk for AI due to the large number of migratory birds crossing the territories and the high risk of spreading the infection among domestic poultry. In April, FAO/WHO confirmed AI H5N1 presence in 8 locations in Gaza and preventive culling was concluded in the infected areas. The project aims to strengthen the public and veterinary health sectors to respond to possible future outbreaks and will be implemented jointly with UNDP. The overall responsibility for overseeing and coordinating institutional and implementation arrangements will be vested with the National Emergency Committee for Avian Influenza Control (NCAIC) which is chaired by the Minister of Health.</p>
<p><b>Multi-Donor Trust Fund</b></p>	
<p>Name of Fund</p>	<p>Description</p>
<p><b><i>Emergency Services Support Program</i></b>  Approval Date: August 2006  Closing Date: June 30, 2008  Task Team Leader: David Steel</p>	<p>The development objective of the Emergency Services Support Program is to mitigate the deterioration of service delivery brought about by the inability of the Palestinian Authority to meet its non-salary recurrent costs. The ESSP finances the non-salary expenditures of the key social ministries and based on the PA's recurrent expenditure program for these ministries. Total donor commitments to date equal US\$55 62 million.</p> <p>The ESSP budget is based on the PA's annual recurrent expenditure program. Eligibility of expenditures is assessed by the Bank, taking into account the emergency nature of the project and the Bank's procurement and fiduciary requirements. Financing of expenditures in other sectors may become possible if donors are willing to provide the necessary financing.</p>

# West Bank and Gaza Portfolio

January 1, 2007

(in US\$ Million)

	Trust Fund for Gaza and the West Bank		Co-financing		
CURRENT PROJECTS	Committed	Disbursed	Committed	Disbursed	Total Disbursed
01 Solid Waste and Environmental Management Project	9.5	7.3			7.3
02 Integrated Community Development Project	15.0	8.5			8.5
04 Emergency Water Project	12.5	7.0			7.0
04 Social Safety Net Project	10.0	1.0			1.0
05 North Gaza Emergency Sewage Treatment Project	7.8	4.3	14.0	0.0	4.3
05 Land Administration Project	3.0	0.5	1.5	0.5	1.0
05 Tertiary Education Project	10.0	1.8	5.9	0.3	2.1
05 Gaza II Emergency Water Project	20.0	7.2			7.2
07 Avian Influenza Project	10.0	0.0			0.0
07 Palestinian NGO Project III	10.0	0.0			0.0
07 Emergency Municipal Services Rehabilitation Project II	10.0	0.0			0.0
<b>Total</b>	<b>117.8</b>	<b>37.6</b>	<b>21.4</b>	<b>0.8</b>	<b>38.4</b>
COMPLETED PROJECTS	Committed	Disbursed	Committed	Disbursed	Total Disbursed
00 Electricity Sector Management Project	15.0	14.8			14.8
03 Emergency Services Support Project II	40.0	40.0	71.6	71.6	111.6
97 Palestinian Expatriate Professional Program	2.3	2.3	0.3	0.3	2.6
02 Emergency Services Support Project	20.0	20.0	29.2	29.2	49.2
04 Public Financial Management Reform SAO	20.0	20.0			20.0
97 Legal Development Program	2.8	2.5			2.5
96 Municipal Infrastructure and Development Project	40.0	40.0	5.4	5.4	45.4
97 Microenterprise Project	2.2	2.2			2.2
95 Emergency Rehabilitation Project	30.0	30.0	63.9	63.9	93.9
97 MIGA Fund	10.0	10.0			10.0
96 Emergency Rehabilitation Project II	20.0	20.0	3.5	3.5	23.5
97 Community Development Project	10.0	10.0	2.8	2.8	12.8
01 Emergency Response Program	12.0	12.0			12.0
95 Education and Health Rehabilitation Project	20.0	20.0	29.1	29.1	49.1
99 Community Development Project II	8.0	8.0			8.0
97 Gaza Water and Sanitation Project	31.0	31.0			31.0
98 Palestinian NGO Project	10.0	10.0	4.6	4.6	14.6
99 Bethlehem 2000	25.0	25.0	3.6	3.6	28.6
97 Palestinian Housing Project	17.4	17.4			17.4
98 Gaza Industrial Estate	7.2	6.9			6.9
99 Southern Area Water and Sanitation Project	21.0	21.0			21.0
00 Health System Development Project	7.9	7.9			7.9
01 Education Action Project	7.0	7.0			7.0
03 Emergency Municipal Services Rehabilitation Project	20.0	20.0			20.0
01 Palestinian NGO II Project	8.0	8.0	11.6	11.6	19.6
00 Municipal Infrastructure and Development Project II	7.5	7.5			7.5
<b>Total Completed</b>	<b>414.2</b>	<b>413.5</b>	<b>225.7</b>	<b>225.7</b>	<b>639.2</b>
<b>TOTAL (Current &amp; Completed)</b>	<b>532.0</b>	<b>451.1</b>	<b>247.1</b>	<b>214.1</b>	<b>665.1</b>
DONOR FUNDED TRUST FUNDS					
The Holst Fund**			273.4	273.4	273.4
Technical Assistance Trust Fund**			23.6	23.6	23.6
PEACE Facility**			25.0	25.0	25.0
Public Financial Management Reform Trust Fund**			273.4	273.4	273.4
Emergency Services Support Program			62.0	9.0	9.0
<b>TOTAL DONOR FUNDED TRUST FUNDS</b>			<b>657.4</b>	<b>604.4</b>	<b>604.4</b>
<b>GRAND TOTAL</b>	<b>532.0</b>	<b>451.1</b>	<b>904.5</b>	<b>818.5</b>	<b>1,269.5</b>

\* For some cofinancing, investment income is added to the principal and disbursed, causing disbursements to go above 100%

\*\* Closed

2/ Year approved by World Bank Board of Executive Directors

# Emergency Services Support Program (ESSP)

The Emergency Services Support Project (ESSP) was launched in 2002 to mitigate the effects of economic crises by financing non-salary recurrent expenditures of the ministries of health, education and higher education and social affairs, and by providing financial support to municipalities. Between March 2002 and June 2005, ESSPI and II financed to a total of US\$176 million from Bank and donor resources.

In response to the recent fiscal crisis, the Bank has re-launched the ESSP. As of today, \$62 million have been pledged by nine donors (Austria, Belgium, DFID, EC, Norway, Spain, France, Switzerland and Sweden). The Bank has signed Administration Agreements (AAs) with the nine donors for a total of US\$ 62 million, of which \$58 million have been transferred to the Bank (see Table 1).

A total of \$23 million has been committed to date (40% of available budget). It is projected that a total of \$51.5 million, representing 92% of the budget available from donor commitments, would be fully committed by March 31, 2007 (see Table 2). A total of \$10 million has been disbursed to date, including direct payments made through the Bank and payments made through the Special Account held by the Office of the President (OoP). The ESSP relies on implementation by the line ministries, with supervision, financial control and disbursements by the OoP. The ESSP involves 113 procurement packages, and a substantial amount of incremental operating expenditures.

In health, 9 packages for drugs estimated at US\$3.3 million will be signed in January, with delivery in February and March 2007. An ICB package about \$7.9 million is expected to be signed in February 2007, with delivery in March 2007. In addition, \$6 million have been allocated for contracting of specialized health services with 42 NGO health care providers, and \$5 million for incremental operating costs. In Education, \$5.7 million has been paid for university staff fees. Out of 41 procurement packages, 25 are in an advanced stage of the procurement, and the remaining 16 will be under procurement in January 2007. In Social Affairs, there are 14 procurement packages with an estimated value of \$600,000. Of these, 11 contracts were signed in December 2006, and the remaining 3 contracts are planned for signing by end of January 2007. Most goods procured under these contracts (e.g., food) will be delivered on a monthly basis.

Upon the request of DfID, the Bank has widened the scope of the ESSP to include operation and maintenance costs in power and water/sanitation. DfID and the Bank have signed a revised AA for an additional US\$5.5 million towards these sectors. Priority expenditures have been identified by the utilities, and the first disbursements are underway. The OoP will supervise and make payments, while the daily implementation will be carried out by the Palestinian Energy Authority (PEA), the local Power Utilities, the Palestinian Water Authority (PWA) and the Coastal Municipal Water Utility (CMWU).

## ESSP Facts and Figures

### Estimated Budget

Requirement (one year) \$111.5 mn

*Education:* \$37.9 mn

*Health:* \$57.7 mn

*Social Affairs:* \$2.0 mn

*WatSan/Power:* \$12.0 mn

*OoP Project Management:* \$ 0.8 mn

Donor Commitments: \$62.0 mn

### Eligible Expenditures

*All ministries:* Rent (buildings, schools, health clinics, shelters), transportation, fuel, insurance, licensing, utilities, office supplies, maintenance.

*Health:* essential drugs, vaccines, lab/blood bank materials, medical consumables; maintenance and rental of facilities, hospital cleaning/food contracts, contracts with non-governmental institutions providing services.

*Education:* examination costs (materials/stationary/monitoring), school supplies, vocational training materials, minor school rehab, recurrent expenses for universities, including some staff salaries.

*Social Assistance:* basic furniture, equipment for shelters and rehab centers, minor rehab works on shelters/centers, and food for residents of shelters/centers.

*Water and Sanitation/Power:* basic goods and services directly related to the operation & maintenance of the networks.





# “Doing More”

## World Bank New Projects

### NGO Project III:

The objective of the project is to provide social services to those who are poor, vulnerable or affected by the deteriorating socioeconomic conditions by establishing an effective mechanism to improve the quality and sustainability of NGO social service delivery. The project has also been designed to contribute towards institutional development of the NGO sector and contribute to equity in access to social services for the poor and marginalized. The total project costs have been estimated at US\$17.60 million, with financing of US\$10 million from the Trust Fund for Gaza and West Bank (TFGWB) and €6 million by the Agence Française de Développement (the French Development Agency).



### Emergency Municipal Services and Rehabilitation Project II:

The impact of prolonged economic contraction and fiscal compression has been felt across all segments of Palestinian society and at every institutional level. Due to lack of fiscal transfers, municipalities have been unable to sustain municipal services. The main objectives of EMSRP II are to: (a) help mitigate further deterioration in the delivery of essential municipal services (ii) create temporary job opportunities at the local level through the launching of labor-intensive employment generation schemes, and (iii) pilot innovative initiatives that foster Local Government-NGO collaboration in response to urgent community needs and assist municipalities in recovering costs for the provision of services. The total cost of the proposed project is currently estimated to be about US\$40.2 million out of which US\$10 million with financing of US\$10 million from the Trust Fund for Gaza and West Bank (TFGWB), and further commitments of €5 million from the Government of the Netherlands and €12 million from Agence Française de Développement. Other donor funding commitments are pending.

### Supplemental Financing for the Integrated Community Development Project (ICDP):

The ICDP is a follow-on project to the previous CDPI & II, aimed at improving the quality and availability of basic social and economic services in poor and marginalized communities through financing investments in local infrastructure and institutions. ICDP prioritizes investments to preserve and extend the capital stock of infrastructure owned by villages and small municipalities in regions with the highest incidence of poverty. The proposed additional financing of US\$5 million from the Trust Fund for Gaza and West Bank (TFGWB) would increase investments in local infrastructure and institutions to improve the quality and availability of basic social and economic services, promoting local economic growth and employment, and supporting human development and poverty reduction. Priority will be given to projects with the highest labor content (above 30 %) and which reach the most communities.



# Announcement



## World Bank **Energy Report**

The West Bank and Gaza (WBG) Energy Sector Review will examine how the energy sector can make an effective contribution to WBG's recovery and long-term growth. It will therefore generally deal with activities and issues relevant to the medium to long term outlook, but it will also include an assessment of more immediate issues for the energy sector. It will assess options for achieving objectives for energy service delivery under the current constraints on budget allocation and investment attraction. It will also develop scenarios that analyze options for expanding and diversifying sources of energy supply in order to guide discussions about long-term priorities and strategy in the sector. The draft Review is scheduled to be discussed with the Palestinian Energy Authority in late-March 2007.

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## World Bank **Transport Report**

In November 2006, the World Bank transport team began the preparation of a Transport Sector Review and Strategy for the West Bank and Gaza. This work was in response to a request from the Ministry of Transport to assist in formulating a strategy for the development of the sector and to enable it to contribute more effectively to the Palestinian economic development. The final report will present the strategy covering an interim period (2007-2009) and a medium term (2010-2012) will focus on issues such as: a) transport issues within the West Bank as well as the linkage with Gaza, and other transport infrastructure and facilities such as the airport, seaport, and the Rafah border crossing; b) institutional and regulatory framework; and c) identification of a priority investment program that would provide the international donor community a coherent framework to coordinate its financial support. The planned completion of this work is May 25, 2007.



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