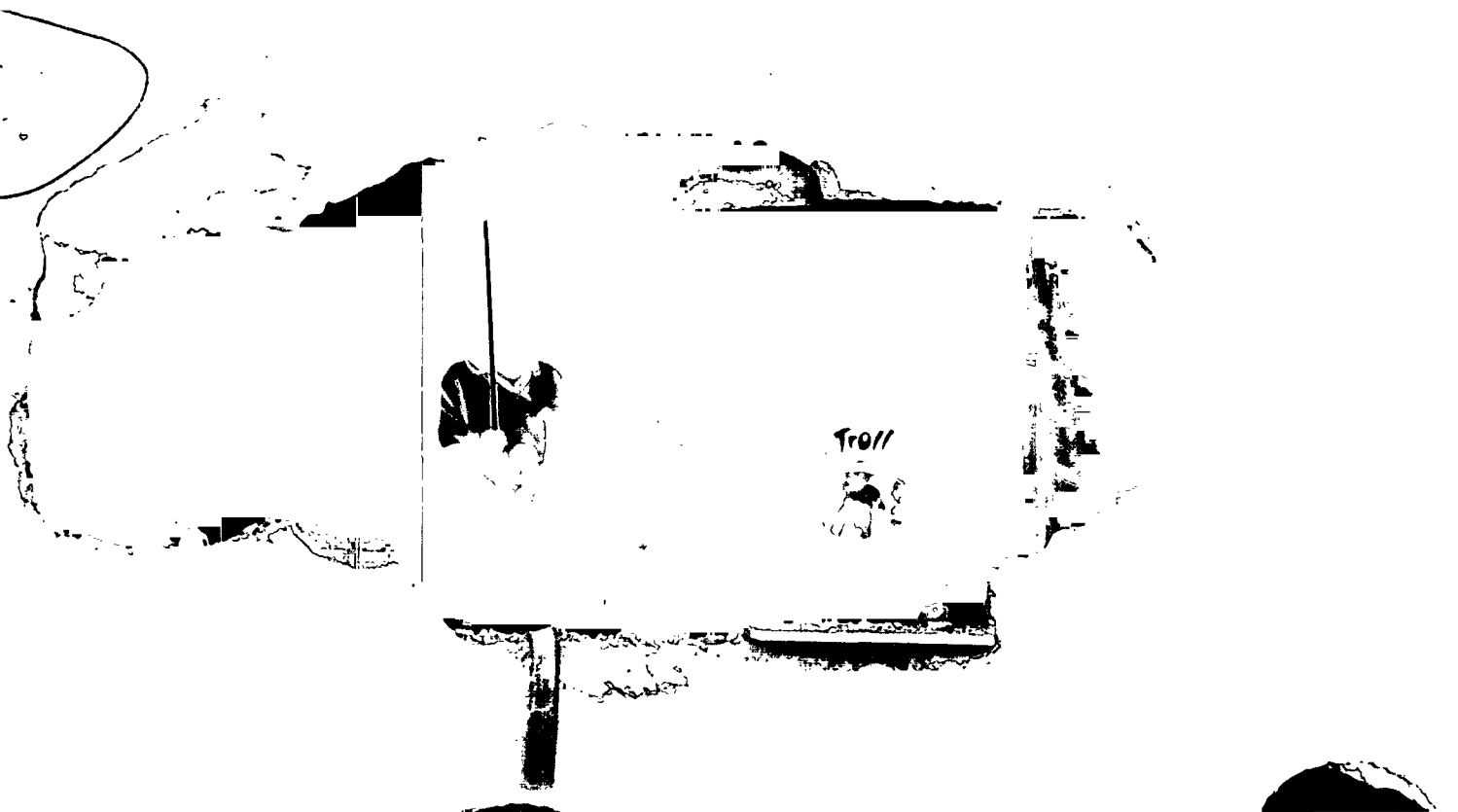


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Fifteen Months - Intifada, Closures and **Palestinian Economic Crisis** An Assessment



World Bank, March 2002

**Fifteen Months – *Intifada*, Closures and
Palestinian Economic Crisis**

An Assessment

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PREFACE

“*Fifteen Months – Intifada, Closures and Palestinian Economic Crisis: An Assessment*” (the *Assessment*) was prepared at the request of the donor community. It is intended to help donors and the Palestinian Authority (PA) cope with the current economic crisis in the West Bank and Gaza. The report is also an attempt to encourage and inform dialogue between donors, the PA and Israel. While it focuses on immediate emergency issues, it recognizes the need to balance short-term measures with a continued commitment to the longer-term institutional and development agenda.

Since the beginning of the *intifada*, donors have been heavily involved in providing emergency assistance to the PA and the Palestinian people. By mid-2001, however, many donors felt they needed a better sense of the economic impact of the crisis, and suggestions on what priorities they should address in 2002.

Working under the aegis of the Local Aid Coordination Committee, the World Bank prepared this report with technical cooperation from UNSCO and financial support from the Government of Norway. The exercise has been extensively discussed with donors and the PA and has benefited from numerous comments from these parties. Particular mention should be made of the Technical Committee of all PA ministries and agencies convened by the Ministry of Planning and International Coordination, under the chairmanship of Vice-Minister Samih El-Abed. This Committee interacted with Bank staff and prepared extensive, in-depth comments on an earlier draft. In addition, written comments were received from the following donors and agencies: Belgium, Denmark, the European Commission, France, Germany, the IMF, the Netherlands, Norway, Sweden, the UK, UNCTAD, UNICEF and UNSCO. These comments reflected a broad consensus on the factual basis of the report, its analytical findings and the economic management strategies proposed.

The *Assessment* is notable for the specific commitments of the Palestinian Authority to a program of emergency response and to the reactivation of structural reforms underway on the eve of the *intifada*, and which have slowed as a consequence of the emergency. Text embodying these commitments is found in **Chapter 5** of the *Assessment*, and the PA’s ownership of these initiatives was confirmed at the meeting between Ministers Sha’ath (Planning and International Cooperation), Nashashibi (Finance) and Masri (Economy and Trade) and Joint Liaison Committee donors on November 29, 2001.

At the outset, six working groups were set up to prepare inputs for the *Assessment*. They included Palestinian experts, PA officials and donor staff, and worked from August through October 2001 to collect the information that underpins this report. The six groups tackled the following themes:

- The fiscal situation of the PA and the municipalities
- The extent of social hardship and the impact of emergency alleviation measures

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- The state of the basic social service network
- The impact of the crisis on the private sector
- The extent of physical damage from the confrontations
- The impediments to project implementation and the donor response to the crisis

As expected, the various groups faced difficulty in moving freely in the West Bank and Gaza, and encountered serious data deficiencies in both the public and private sectors. Poor data are a feature of economic work in the West Bank and Gaza, and the current crisis has further compromised existing information systems.

Many people contributed to this report. The main authors of the final paper were Sébastien Dessus and Nigel Roberts of the World Bank. Other contributors are listed below.

Coordination and Editing: Srish Kumar, Consultant, Elizabeth Cousens, UNSCO, Stefano Mocchi, World Bank, Brigitte Petit, World Bank.

Working Groups: Macro-Fiscal/Municipal Finance: Salam Fayyad, IMF, Karim Nashashibi, IMF, Khaled Islaih, UNSCO, Sébastien Dessus, World Bank, Claus Astrup, World Bank, Kingsley Robotham, World Bank. Social Hardship and Alleviation: Paola Cirillo, OCHA, Ray Dolphin, OCHA, Ibrahim Dajani, World Bank, Marisa Kemper, UNSCO, Arjan van Houwelingen, UNSCO, Mohammed Shaheen, Consultant, Ali Mansour, Consultant, Salah Abel Shafi, Consultant. Social Services: Akiko Maeda, World Bank, Salam Kanaan, World Bank, Sima Kanaan, World Bank, Hossam K. Sharkawi, Consultant. Private Sector: Youssef Habesch, IFC, Rami Khoury, IFC, Tamara Lansky, IFC, Matthew Lovick, Cooperative Housing Foundation, Naser Abdel Karim, Consultant, Sherene Abdul Hadi, Consultant, Qais Saleh, Consultant, Samer Irshaid, Consultant. Physical Damage: Majed El-Bayya, World Bank, Thierry Sagaspe, Consultant, Rifaat Rustom, Consultant, Ismael Mahfouz, Consultant, Omar Simo, Consultant, Adnan Abu Humos, Consultant, EMCC Gaza, Consulting Firm, Universal Group, Consulting Firm. Impediments to Project Implementation/Donor Response: Ma'moon Sbeih, World Bank, Julianne Engel, Consultant, Jean-Marie Stratigos and Amina Hamshari, UNSCO.

ABBREVIATIONS AND ACRONYMS

AHLC	Ad-Hoc Liaison Committee	NCPA	National Commission for Poverty Alleviation
BOP	Balance of Payments	NGO	Non-Government Organization
CIDA	Canadian International Development Agency	NIS	New Israeli Shekels
CPI	Consumer Price Index	O&M	Operations and Maintenance
EPF	Economic Policy Framework	OCHA	Office for the Coordination of Humanitarian Affairs
EU	European Union	PA	Palestinian Authority
FAFO	Institute for Applied Social Science (Norwegian Acronym)	PARC	Palestinian Agricultural Relief Committee
FIAS	Foreign Investment Advisory Services	PCBS	Palestinian Central Bureau of Statistics
G	Gaza	PDP	Palestinian Development Plan
GDP	Gross Domestic Product	PECDAR	Palestinian Economic Council for Development and Reconstruction
GHI	Government Health Insurance	PLC	Palestinian Legislative Council
GIE	Gaza Industrial Estate	PLO	Palestine Liberation Organization
GNI	Gross National Income	PMA	Palestinian Monetary Authority
GNP	Gross National Product	PRCS	Palestinian Red Crescent Society
GOI	Government of Israel	SME	Small and Medium Enterprises
ICBS	Israel Central Bureau of Statistics	SWG	Sector Working Group
IDB	Islamic Development Bank	TAP	Tripartite Action Plan
IFC	International Finance Corporation	TFPI	Task Force on Project Implementation
ILO	International Labour Organization	UNDP	United Nations Development Programme
IMF	International Monetary Fund	UNRWA	United Nations Relief and Works Agency for Palestine Refugees in the Near East
JLC	Joint Liaison Committee	UNSCO	Office of the United Nations Special Coordinator for the Middle East Peace Process
LACC	Local Aid Coordination Committee	USAID	United States Agency for International Development
MAS	Palestine Economic Policy Research Institute (Arabic Acronym)	VAT	Value Added Tax
MLG	Ministry of Local Government	WB	West Bank
MOE	Ministry of Education	WBG	West Bank and Gaza
MOET	Ministry of Economy and Trade	WFP	World Food Programme
MOF	Ministry of Finance	WHO	World Health Organization
MOH	Ministry of Health		
MOE	Ministry of Higher Education		
MOI	Ministry of Industry		
MOPIC	Ministry of Planning and International Cooperation		
MOSA	Ministry of Social Affairs		

EXECUTIVE SUMMARY

1. At the signing of the Oslo Declaration, it was well-understood that peace would only take root if there were significant, sustained improvements in the economy of the West Bank and Gaza (WBG). Since October 1993, donor pledges have resulted in US\$6.5 billion in commitments and some US\$4.4 billion in disbursements to the WBG. At US\$195 per person per annum since 1994, aid flows to WBG represents one of the highest levels of per capita official development assistance anywhere in the world. Today, though, the value of this enormous collective effort is threatened by the breakdown in the peace process.

2. The Palestinian economic recovery that began in 1998 came to an abrupt halt with the start of the *intifada* in September 2000, and the subsequent imposition of tight closure. The economy has been decimated over the past fifteen months. Once again, though, donors have demonstrated the importance they attach to a resolution of the Israeli-Palestinian conflict through the efforts they have made to sustain the Palestinian economy and its governance structures.

The Problem

3. **The Palestinian economy is in severe recession.** Per capita real income declined by 12 percent for 2000 as a whole, and by a further 19 percent in 2001. The share of the Palestinian population living below the poverty line (US\$2 per person per day) is currently estimated at 45-50 percent. While the human losses to death and injury defy economic estimation, raw physical damage from the conflict is estimated at US\$305 million as of the end of December 2001.¹ Far more significant, though, are Gross National Income losses, which amounted to at least US\$2.4 billion in real terms by the end of 2001. Average per capita real income is now 30 percent below what it was when the Gaza-Jericho Agreement was signed in 1994.

4. **The proximate cause of the Palestinian economic crisis is Israel's closure of the Palestinian territories.** Only a drastically reduced number of Palestinian workers is permitted to work in Israel and the settlements, and the flow of goods into and from the Palestinian areas has been severely interrupted. Military checkpoints exist on all main and most secondary roads within the West Bank and Gaza, hampering internal communication. Periodically, all traffic from and within the territories is shut down, and many communities have experienced prolonged periods of isolation. These closures have raised economic costs and have crippled the business environment.

5. **The Palestinian economic decline has been driven by unemployment in the private sector.** Since September 2000, 75-80,000 Palestinians have lost their jobs in Israel and the settlements, while another 60,000 jobs have been lost inside the Palestinian territories as demand collapsed and businesses were forced to lay off workers. With more than 100,000 joining the

¹ Consisting of damage to houses and furnishings, public infrastructure, commercial properties and plant, and agricultural land including trees, wells, and irrigation systems.

working-age population in the course of the *intifada*, unemployment has climbed from 10 percent of the Palestinian workforce in September 2000 to 26 percent today (35 percent using a more relaxed definition of unemployment).

6. **The Palestinian Authority (PA) is effectively bankrupt, since tax revenues have dwindled to one fifth of previous levels.** Monthly budget needs under the “austerity budget” promulgated in March 2001 total US\$90 million, but revenue collected by the PA now amounts to less than US\$20 million per month (compared with an average of US\$88 million per month in the third quarter of 2000). Under normal circumstances, about two-thirds of Palestinian revenue derives from taxes collected by Israel on the Palestinian Authority’s behalf. In the past, these taxes were remitted to the PA on a regular basis, but no such payments have been made by Israel since December 2000. Total gross revenues withheld by Israel are estimated as of end-December 2001 at NIS 2.1 billion -- or approximately US\$0.5 billion.

7. **A full collapse of the economy and government has been averted, however.** After three months of economic freefall in the last quarter of 2000, the situation stabilized somewhat, and the rate of decline has subsequently been slower. There are four main reasons for this.

8. First, the Palestinian Authority has tightened its belt and managed the crisis well, particularly in the fiscal and service delivery spheres. Second, after a virtual cessation of work in Israel in the first weeks of the *intifada*, an average of 50,000 workers from the West Bank have managed to find work again (without permits) in Israel and the settlements. Third, households have reduced their expenditures and drawn down their savings, and informal self-help and sharing systems have redistributed the economic pain. And fourth, the donors (often working through NGOs) have injected timely and generous emergency assistance.

9. **Despite the difficulties of working in conflict, donor funding has increased dramatically. Compared with 1999, commitments rose by 77 percent and disbursements by 93 percent in 2001.**² Over 80 percent of 2001 disbursements were devoted to budget support and emergency relief. By mid-2001, Arab League donors were contributing US\$45 million a month in budget support (through the Islamic Development Bank), while the European Union has been providing another US\$9 million per month.³ This unprecedented quantity of budget support has helped sustain a minimum level of demand and has prevented the disintegration of government structures. Donor contributions to UNRWA have also been key, and numerous small-scale workfare programs for the newly unemployed have been put in place (with Germany, the US and the World Bank as major contributors). Without the intervention of the donors, and in particular the Arab League and European Union states,⁴ all semblance of a modern economy would have disappeared by now. Even so, the surge in assistance comes with a price – disbursements on

² 1999 was the last full pre-*intifada* year. Donor commitments totaled US\$692 million in 1999, US\$973 million in 2000 and US\$1,228 million in 2001; disbursements totaled US\$482 million in 1999, US\$549 million in 2000 and US\$929 million in 2001.

³ Total budget commitments through the end of 2001 from donors amount to US\$584 million: US\$405 million from Arab League members through the IDB, US\$114 million from the EU, and contributions of US\$40 million from Saudi Arabia, US\$15 million from the UAE and US\$10 million from Norway.

⁴ Together, they accounted for 68 percent of 2001 disbursements. Of the US\$929 million disbursed, US\$388 million (42 percent) was disbursed by the Islamic Development Bank on behalf of Arab League states, and US\$245 million (26 percent) by the European Union (Commission and member states). The USA disbursed another US\$114 million (12 percent).

growth-oriented infrastructure and capacity building projects dropped from over US\$400 million in 1999 to US\$175 million in 2001, and many large capital projects (highways, industrial estates, the port, the Gaza airport) have been seriously delayed or damaged. In effect, long-term investment has been sacrificed to short-term survival.

10. **However, the current situation is unstable, and economic disintegration continues.** In the past two months, closure and conflict have once again intensified. Households have in many cases exhausted their savings and their capacity to borrow. Emergency employment schemes, for all their merits, have not made a significant dent on unemployment.⁵ The fiscal situation continues to deteriorate, and donor contributions have not closed the budget deficit. Up to now the PA has managed this deficit by borrowing from commercial banks, cutting salaries, squeezing operating costs and delaying the payment of bills. All of these strategies are reaching their limits. By the end of 2001, the PA's arrears amounted to US\$430 million, most of these to commercial suppliers; this in turn has increased the number of non-performing loans and is placing great stress on the commercial banking system.

11. **If closure is tightened further, current PA, community and donor efforts will not suffice, and the economy will unravel.** Soon little will remain of the private sector other than subsistence agriculture, petty trade and workshop manufacturing. Public services will break down, with trash accumulating, frequent power and water cuts, intermittent drug supplies in hospitals and a shortage of textbooks and writing paper in schools. Notably vulnerable are the municipalities, which have received little emergency support and are in many cases in debt to Israeli utility companies. Poverty is deepening, particularly in isolated communities. Serious health and environment problems are emerging. Helplessness, deprivation and hatred are increasing.

12. **A political solution would alter this prospect fundamentally,** and a rapid recovery of the Palestinian economy would accompany a lifting of closure. Even so, World Bank projections indicate that recovery to pre-*intifada* per capita income levels would take at least two years – assuming that private investor confidence can be restored.

The Way Ahead

13. **Israel, the PA and the donors will all need to play their parts if the situation is to be reversed.**

14. **Any significant recovery of the Palestinian economy requires that the system of internal checkpoints be dismantled and border restrictions eased. It also assumes that the Israeli labor market will be re-opened to Palestinians.** These actions would lower the costs of doing business and would stimulate a recovery of Palestinian private enterprise.

15. **In addition, the tax revenues that have been withheld from the Palestinian Authority would need to be released, and regular revenue clearances resumed.**

⁵ In 2001, some 10,000 full-time job equivalents were created under these programs. The total number of unemployed in WBG (excluding East Jerusalem) was estimated in end-2001 at some 264,000 (using the relaxed definition of unemployment).

16. The donors need to provide a major program of emergency support for 2002. It is recommended that this support focus on seven packages of assistance. **Taken together, these packages would provide a solid basis for an eventual resumption of growth:**

- **Budget Support.** This must be continued through the year. The IMF has estimated needs at US\$924 million under a *status quo* scenario. If closure were lifted and if Israel resumed regular revenue transfers to the PA, the requirement would fall to between US\$360-420 million. The key sources remain the Arab League states and the EU.
- **Basic Services.** Targeted assistance for basic service delivery and for the key institutions responsible for delivering them is needed; the agencies include the Ministries of Health, Education and Social Affairs, and the municipalities. An Emergency Services Support Program (ESSP) has been designed for this purpose and would need c. US\$155 million for 2002⁶ under a *status quo* scenario. The aim of the ESSP is to address the severe shortages of drugs, school materials, and spare parts/fuel for water, electricity and solid waste collection systems.
- **Re-engaging the Private Sector.** Two programs are proposed for this neglected but essential area. Due to the fiscal crisis, the PA has not been able to process VAT refunds to suppliers, and this could be addressed through a concessional loan of c. US\$35 million to the PA in the event that Israel continues to withhold revenues owed. The International Finance Corporation is working with the PA and other donors to design a Crisis Fund to provide immediate support to businesses, as well as during any future recovery phase. At present many businesses remain viable but need advice on how best to manage the crisis. They also need access to capital to diversify activities and exploit export opportunities. Others have lost buildings, inventory and equipment in the fighting, and need reconstruction assistance. Many others, however, cannot be meaningfully assisted until there is a resurgence of demand. Under a *status quo* scenario, US\$40 million would be sought to provide support now, and a further US\$100 million to finance the recovery phase.
- **Unemployment and Welfare.** Cash payments and job creation schemes will be needed to deal with persistent unemployment and hardship in 2002. It is recommended that the PA and the donors carry out a joint stock-taking exercise to assess experience with job creation and cash transfer programs in WBG, with a view to achieving consensus on how to crystallize the technical lessons learned so far, and on how to scale up existing efforts. Several proposals for the creation of special funds have been made by different PA officials in recent weeks, and the merits of these should be considered as part of this exercise. Under *status quo* some US\$200 million would be needed for unemployment schemes and cash payments in 2002.
- **Infrastructure and Land Rehabilitation.** Donor reconstruction and rehabilitation funding of somewhere between US\$125 million and US\$200 million would be justified to restore the areas damaged by armed conflict, with due consideration given to the extent to which

⁶ Of which US\$96 million would contribute to the central PA budget (and would replace part of the US\$924 million otherwise needed).

armed conflict has subsided. Various of the works can be packaged by area, sector or theme should individual donors prefer this.

- **Student Scholarships.** These could be provided to pupils and students unable to pay school/university fees, as a way of supporting their continuation in study and sustaining the financial viability of institutions of learning. A notional allocation of US\$20 million is proposed under *status quo*.
- **UNRWA.** The refugee population in WBG remains heavily dependent on UNRWA for basic social services and welfare payments. UNRWA's Third and Fourth *Intifada* Emergency Appeals are still under subscribed by some US\$142 million, and donors should try to fund the gap.

17. Total donor financing needed for 2002 varies according to the political scenario projected. Should the peace process resume and closure be lifted, total needs would amount to about US\$1.1 billion. A continuation of the *status quo* would require around US\$1.5 billion from donors, and a significant further tightening of closure would increase total emergency needs to around US\$1.7 billion.

18. **Donors must also re-dedicate themselves to the medium-term development agenda.** Most major infrastructure work has stalled, and many capacity building exercises have languished, in part because of the difficulty of retaining or recruiting qualified experts. Donors who have been most effective in implementing field programs during the *intifada* are by and large those whose programs work closely with local communities. The exigencies of the operating environment offer an opportunity here, since decentralized programs, if well-supported and monitored, can result in better poverty targeting, higher local content, and the strengthening of accountability.

19. **For its part, the Palestinian Authority will need to maintain strong budget discipline in 2002 and make adequate provision for essential operating costs, as well as work further on prioritizing emergency support needs.** The PA intends to develop a Palestinian Emergency Plan for 2002 with strong participation by civil society, as a way to focus Palestinian energies on economic survival and recovery. In addition, the PA has committed itself to concerted efforts to rationalize the roles and develop the systems and capacities of the three economic ministries – Finance, Planning and International Cooperation and Economy and Trade.

20. **The PA has also indicated that it will recommit itself to the medium-term institutional and policy agenda that has been largely in suspense since September 2000.** This agenda has two main planks – the promotion of transparency and accountability in the public sector, and the creation of a supportive environment for private sector development. Measures to which the PA has restated its commitment include:

- the continued consolidation of all sources of revenue in a single treasury account, and the maintenance of a public sector hiring freeze.⁷

⁷ With the exception of essential teachers, health workers and judicial staff.

- the common application of public procurement standards and guidelines, and the strengthening of the capacity of the General Control Institution (the public audit entity).
- the development of a unified pension system covering all public employees, as a precursor to a program of civil service “down-sizing” once the current crisis is past.
- the creation of a legal environment conducive to investment, by presenting to the Palestinian Legislative Council (PLC) a portfolio of laws which include a Capital Markets Authority Law, an Insurance Law, a Securities Law, a Companies Law, a Secured Financing (Leasing) Law and an Income Tax Law.
- ensuring adequate commercial competition, by accelerating the establishment of a Palestinian Investment Fund to oversee the privatization of PA assets, in particular quasi-monopolistic trading activities -- and by presenting to the PLC a Competition Law.
- ensuring that contracts are enforced and that investors are given proper legal protection, through improving the functioning of the courts and by enhancing the skills and independence of the judiciary.

21. **This important agenda should now be implemented.** The PA recognizes that statements of commitment to reform are of limited value if not translated into action. Accordingly the PA will, by March 31, develop a detailed Action Matrix featuring the various reforms described above and assigning responsibilities and delivery dates.



1. PROLOGUE

1.1 Nearly 1,100 people died as a result of the conflict between September 28, 2000 and early December 2001, and nearly 19,000 were injured. Of the dead, 860 were Palestinian and 218 Israeli; of the injured, 16,780 were Palestinian (some 2,500 of whom are expected to suffer permanent disability),⁸ and 2112 Israeli.⁹ Countless others in Gaza, the West Bank and Israel have been traumatized and will suffer long-lasting emotional damage. It is against this background of human suffering that the *Assessment* attempts to paint an objective picture of the economic impact of the conflict.

1.2 An important reason for donor interest in this report is the damage caused during the past year to the unique process launched in 1993, and to the collective effort to support the reconciliation of the Palestinian and Israeli peoples. At the signing of the Oslo Declaration, it was well-understood that peace would only take root if there were significant, sustained economic improvements in the West Bank and Gaza (WBG). In October 1993, forty-two donor countries and agencies met at a US-sponsored conference to pledge financial support, in one of the broadest and most ambitious international aid efforts in history. Since then, donor pledges have resulted in US\$6.5 billion in commitments and US\$4.4 billion in actual disbursements to the WBG. At about US\$195 per person per year, aid to WBG represents one of the highest levels of per capita official development assistance anywhere in the world.

1.3 The donors have played a central role in WBG, and continue to do so. The challenge for donors has involved helping create a Palestinian administration from scratch, coping with continuous political uncertainty and frequent political and economic shocks, coordinating among themselves and navigating the uncertainties of a unique trilateral relationship (between donors, the PA and the Government of Israel). Given these difficulties, donors, the PA and Palestinian civil society have achieved a great deal, and this has been recognized by the Palestinian public. An *Aid Effectiveness Survey* prepared jointly by Japan and the World Bank for the Ad Hoc Liaison Committee (AHLIC) in 1999 shows a keen public awareness of improvements in the provision of services and in the lives and prospects of the population, and of the donors' seminal contribution to this. By September 2000, the economic decline associated with the violence and closures of 1995-96 had been arrested, and Palestinian economic prospects were relatively positive.

1.4 The events of the last sixteen months have jeopardized this enormous investment of international capital, ideas and effort. As will become apparent, however, it has not extinguished the donor community's belief in the need for a future of peaceful coexistence between Palestinians and Israelis. One of the key building blocks for this remains a viable Palestinian

⁸ Of the total Palestinian dead, three-quarters fell into the 19-49 age bracket. Of the injured, 60 percent were between 19 and 49.

⁹ Sources: *Palestinian Red Crescent Society*, December 9, 2001; *B'Tselem*, December 3, 2001.

Fifteen Months – Intifada, Closures and Palestinian Economic Crisis – An Assessment

economy, and orderly economic cooperation between Israel and the Palestinian Authority – a premise reinforced by its absence during the past year. While donors have concentrated their energies on emergency relief, they remain committed to the main agenda of state and institution-building. This report aims to help donors achieve the right balance between needed short-term crisis support and a continued focus on the policies, institutions and infrastructure that can assure sustained economic growth and lay the foundations for a Palestinian state.



2. THE CAUSES OF THE DAMAGE

2.1 This report aims to measure the impact of a year of turmoil on the Palestinian economy and on Palestinian livelihoods. The damage can be ascribed to the impact of two related phenomena – closures and armed confrontation.

CLOSURE

2.2 “Closure” is a term referring to the restrictions placed by Israel on the free movement of Palestinian goods and labor across borders and within the West Bank and Gaza. Closure has come to dominate much of Palestinian life over the past fifteen months.¹⁰

2.3 The restrictions take three basic forms: internal closure within the West Bank and Gaza, closure of the border between Israel and the West Bank and Gaza and closure of international crossings between the West Bank and Gaza and neighboring Jordan and Egypt.

2.4 **Internal closure.** A dense network of fixed and mobile military checkpoints has been established on transportation lines within the West Bank and Gaza since September 28, 2000 (see **Maps**). At times of severe internal closure – 73 percent of the time in the West Bank and 4 percent in Gaza through the end of December 2001 -- pedestrian and vehicle mobility on main roads is reserved for Israeli military personnel, settlers and non-Palestinians, while even on days of “partial” closure these checkpoints have created a life of roundabout routes, interminable delays and frequent harassment.¹¹ As a result, productive time is lost, transport costs have risen, damage to roads and vehicles has increased and the normal intercourse of business and commerce is a thing of the past. For Palestinians living in remote areas of the West Bank, severe internal closure imposes special difficulties, particularly in access to basic services such as health and education; cases of sick and elderly people dying before they can get care have been widely publicized. Internal closure is not distributed evenly, and is to some extent associated with the various “flashpoints” near settlements and military encampments.

¹⁰ The main source for Chapter 2 is UNSCO, *Impact on the Palestinian Economy of Confrontation, Border Closures and Mobility Restrictions*, various issues.

¹¹ Partial internal closure – representing a lesser degree of restriction on travel -- was in force for another 125 days (27 percent) in the West Bank, and another 433 days (95 percent) in Gaza. This generally involved diverting traffic away from settlements. Thus the main north-south road in the West Bank has been inaccessible for most of the reporting period, with circuitous travel via the Jordan Valley required. Internal closure has been more severe in the West Bank, and is used to offset the more porous nature of the border between the West Bank and Israel.

Box 1: Roundabout Routes

Residents are forced to travel circuitously, to walk, to change taxis, to climb paths along hills and between olive orchards, at times trying to retrace their steps due to a suddenly-instituted roadblock now holding back a kilometer's worth of cars, or because of a new closure that wasn't there even the night before.

Source: Ha'aretz, The Long and Winding (Dirt) Road, January 28, 2001.

2.5 Areas that are habitually affected are the Tulkarem/Jenin/Qalqiliya crescent in the north-west West Bank, Nablus and Ramallah/Al-Bireh in the central West Bank, and Jericho, the Bethlehem municipalities and Hebron in the south¹² -- while in Gaza, internal closure has resulted in a radical reduction of north-south travel and has at times created three semi-isolated enclaves (Gaza City, the Jabalia area and Rafah/Khan Yunis).

2.6 Closure has also included restrictions on fishing off the Gaza coast, intermittently imposed throughout the *intifada*.

2.7 **Border closure with Israel.** Since 1993, Palestinians have needed to hold permits from the Israeli military authorities to enter or transit through Israel or East Jerusalem (including for travel between the West Bank and Gaza). Since the beginning of October 2000, the permit regime has been dramatically tightened, with permits frequently cancelled and border crossings intermittently sealed. The impact of these measures has greatly reduced the employment of Palestinians in Israel and the level of consumer demand in WBG. In addition, the movement of goods across borders has been subject to severe and unpredictable interruption.

- *Restrictions on Palestinians entering Israel from Gaza.* The main crossing point between Gaza and Israel was closed for 65 percent of the time between October 2000 and end-December 2001. Even on days when the crossing point was "open," the number of Palestinian workers entering Israel/the settlements from Gaza was less than 20 percent of the pre-crisis level of 29,000, due to permit restrictions.¹³ Border closures eased somewhat after mid-December 2000 and considerably in April and May 2001, but spiked upwards in March and June 2001. The crossing point was effectively closed for much of the June-September 2001 period, except for a few days at the end of September.
- *Restrictions on the movement of goods to and from Gaza.* Of the three commercial crossings in Gaza, Karni/Muntar was closed for only 9 percent of the period from September 2000 until December 2001. Sufa/Qarara was closed until the end of March 2001, but has been open since then on most business days until the last three weeks of September, when it closed again. Erez/Beit Hanun has been closed since September 28, 2000. On 30 days in the reporting period, all three commercial crossings were closed. When open, intensive security checks increased transport costs and reduced the number of truckloads, especially in the last quarter (Q4) of 2000. In 2001 commercial truckload movement has improved somewhat. However, in total, commercial crossings have been closed for more than 60% of all days during the first 15 months of the *intifada*.

¹² Hebron is particularly difficult owing to the intermingling of Palestinian communities and Israeli settlements. A curfew restricting Palestinian residents of the "H2" area to their homes – either for 24-hours or defined periods of the day – was in place for over 130 days through June 2001. UNSCO, *Impact on the Palestinian Economy of Confrontation, Border Closures and Mobility Restrictions, 1 Oct 2000-30 June 2001*.

¹³ These were permits provided to workers in the Erez industrial estate on the Gaza border.

- *Restrictions on Palestinians entering from the West Bank.* The number of permits issued to Palestinian workers decreased substantially, and the pre-intifada flow of 95,000-100,000 laborers crossing dropped to 20,000 in the last quarter of 2000. In the first half of 2001, up to 55,000 laborers were able to return clandestinely to Israel and the West Bank settlements, due in part to the porosity of the borders. These numbers declined in the second half of 2001.
- *Restrictions on the movement of goods to and from the West Bank.* The situation has been easier than in Gaza because of the availability of Israeli-registered trucks that can transport goods without permits. Internal restrictions on movements have meant that some areas of the West Bank were still heavily affected.

Box 2: The Impact of the Crisis on Transport Costs

In June 2001, the World Bank commissioned a local consultancy firm to carry out a survey of households and firms, with the aim of uncovering more precisely what the impact on transport costs of closures has been. In total, responses were obtained from 500 households and 188 firms throughout the West Bank and Gaza.¹⁴ The main findings of the survey are:

- In the West Bank, access to public services – health care facilities and schools – has been seriously hampered: the average distance between home and these public services, the average travel time, and average costs to get there have roughly doubled.
- In Gaza, there has been no significant change in the accessibility of public services except for students' access to university, which – as in the West Bank – has been highly obstructed.

The difference between Gaza and the West Bank can be explained by two factors: The population density in Gaza is much higher than in the West Bank, making access easier to begin with, and internal closures in Gaza have been less severe than in the West Bank.

- The accessibility of workplaces has been greatly reduced in both the West Bank and Gaza. The average time to get to work has almost doubled. In particular workers commuting to workplaces in Israel have suffered.
- As might be expected, households living in rural areas have been more severely affected than households living in urban areas.

Firms have suffered even more than households: The survey indicates that the average time needed to bring products from the production site to an outlet within the West Bank and Gaza is 3 times longer now. The average distance to markets was approximately twice as long in June 2001 as it was a year earlier – 75 kilometers compared to 37 kilometers.¹⁵

Even more significant is it that transport time has more than tripled. The very large increase in both travel distances and time is partly due to the fact that trucks must circumvent checkpoints by using dirt roads. The average cost of transporting a truckload of produced goods has more than doubled, from approximately 170 NIS before the outbreak of the *intifada* to 370 NIS in June 2001.

Firms whose products are destined for external markets have endured significant delays at border crossings to Jordan and Egypt or at the Israeli ports of Haifa and Ashdod, on top of the difficulties in reaching the border

¹⁴ Individuals were interviewed in 29 different locations in the West Bank and 14 in Gaza.

¹⁵ As illustrated below.

Transport Impact on Firms Serving Domestic Markets

	June 2000	June 2001	% change
Distance to Markets (Kilometers)	37.1	74.8	102.0
Transport time (Minutes)	51.0	150.0	208.0
Costs per Shipment (NIS)	169.5	370.0	82.0

crossing in the first place (firms report waiting times at the Damya Bridge to Jordan of up to one week – if the bridge is open to Palestinian products at all). Average waiting times at borders increased from 40 hours to 180 hours, or approximately one week, which makes export of perishable goods infeasible. Consistent with this, firms report a significant increase in the quantity of goods damaged at the border crossings: firms estimate that between 2 and 4 percent of the value of shipments was lost at border crossings before the *intifada*, a figure that has increased to 10-15 percent.

2.8 **Closure between the West Bank and Gaza.** The “Safe Passage” route designed to allow Palestinians to move relatively freely between the West Bank and Gaza, which had been in operation for nearly a year, was closed by Israeli authorities on October 6, 2000 and has not been reopened.

2.9 **Border closure with neighboring countries.** Both passenger and commercial traffic through international crossings has been heavily restricted.

- *Restrictions on people.* The Jordanian border was partially or totally closed to Palestinians for 18 percent of the October 2000-December 2001 period, the Rafah crossing to Egypt was partially or totally closed for 57 percent of the time, while Gaza International Airport was partially or totally closed for 80 percent of the period (the runway has subsequently been destroyed by the Israeli Defense Forces).
- *Restrictions on goods.* The Jordanian border was partially or totally closed to commercial traffic for 83 percent and Rafah for 60 percent of the time, leading to a reduction in imports from Jordan and Egypt. Palestinian access to Israeli ports, the entry points for most non-Israeli products, has been reduced by delays associated with security checks and restrictions on access from the ports to Palestinian territory.

ARMED CONFRONTATION

2.10 While movement restrictions have exerted the most direct impact, frequent armed clashes and confrontations have also disrupted economic activity.

2.11 Apart from deaths and injuries, armed clashes have caused destruction and damage to physical infrastructure. This damage is mostly located in border areas in Gaza, near settlements and army positions in various locations, or in and around PA security buildings in several municipalities. The nature and extent of the damage is detailed in **Chapter 3**. While substantial, the direct impact of physical damage on the economy is far less significant than the effects of closure.

2.12 It is harder to measure the impact of armed confrontation on economic expectations. It is clear, however, that the violence has discouraged private investors and donors from funding growth-oriented projects, and that confidence in the economy has ebbed in the absence of any visible political progress. These issues are explored in **Chapter 3**.

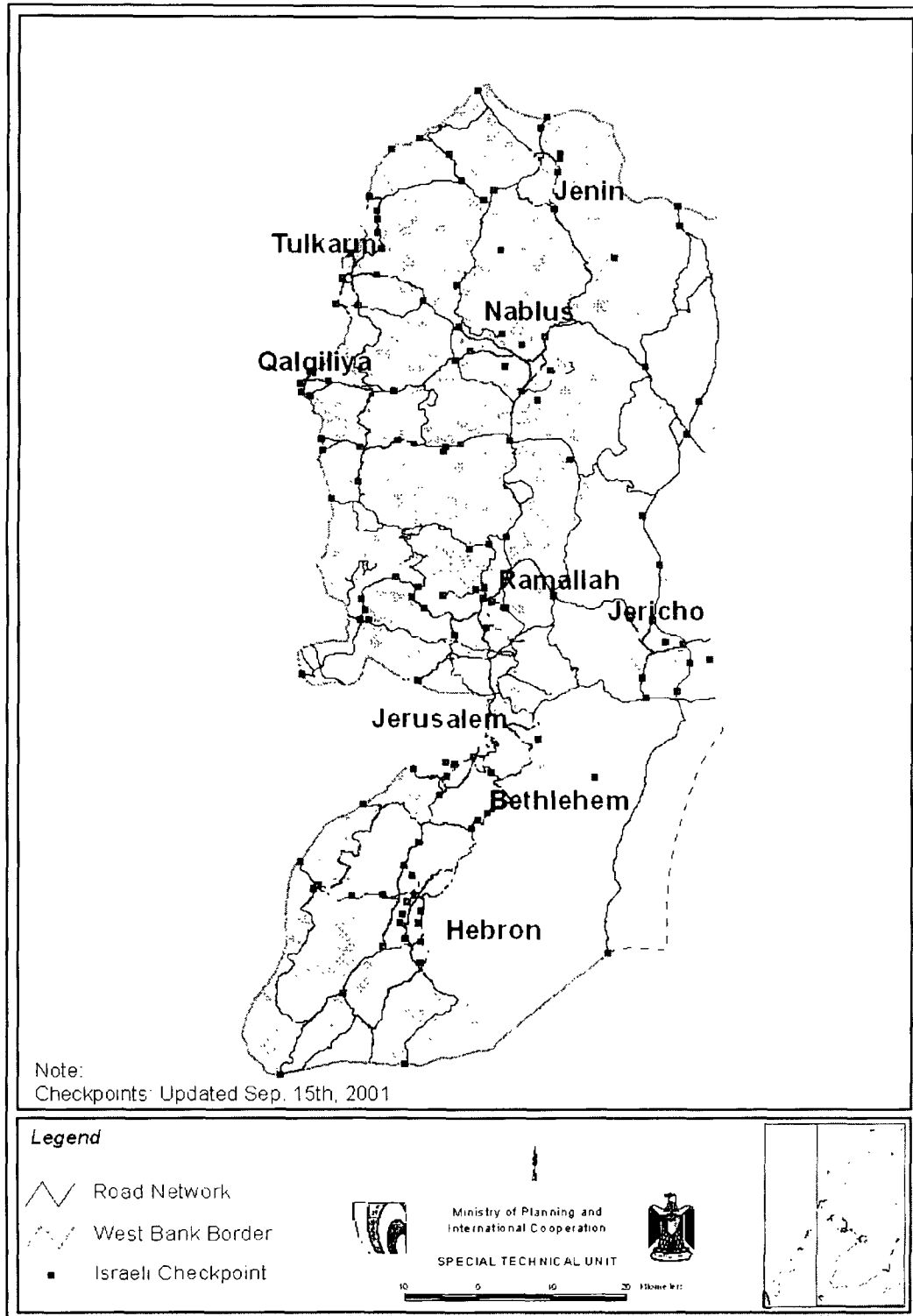
Box 3: Damage from Armed Confrontation – Bethlehem, October 2001

During ten days in October 2001, twenty three lives were lost in the Bethlehem area. Severe physical damage was caused to roads, water and sewage networks, electrical and telecommunication networks, hotels (the Paradise and El Jacir Palace), hospitals, Bethlehem University, agricultural land in rural areas, and private housing and vehicles.

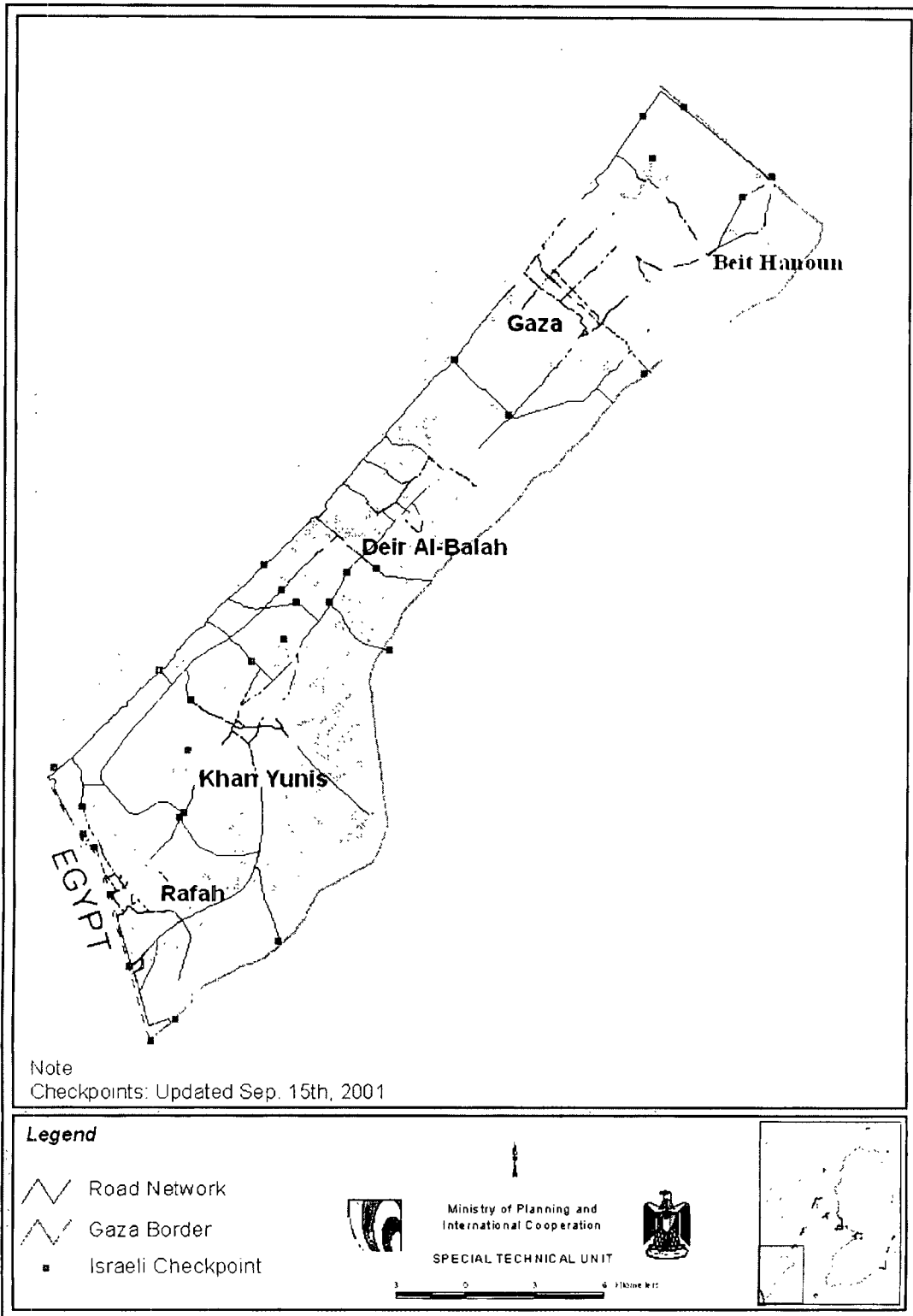
The Bethlehem Governorate formed a committee composed of representatives from the PA, the local municipalities, citizens and professional bodies. This committee had by mid-January assessed damage at 4,298 locations in the Governorate, estimating total losses at US\$16.58 million. Damages in areas B & C could not be assessed for security reasons.

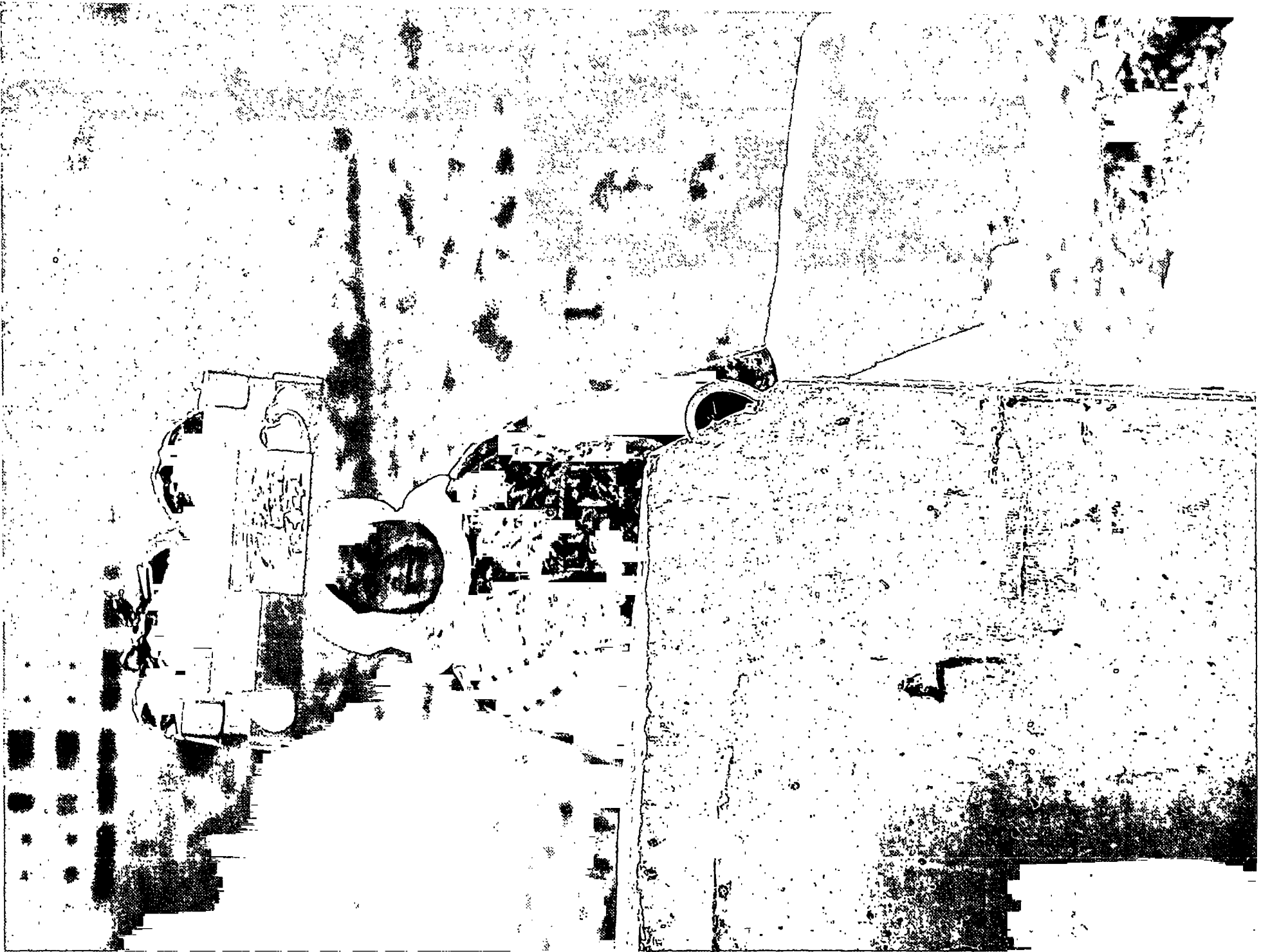
The total includes US\$4.92 million in damage to basic infrastructure (of which US\$0.88 million was to infrastructure recently rehabilitated as part of donor support to the B2000 Project), US\$3.1 million for tourism (the Paradise and El Jacir Palace hotels, the latter a US\$45 million investment in which the IFC is participating), US\$7.44 million for residential buildings, and US\$1.11 million for commercial and industrial buildings.

**Maps of the Checkpoints (as of September 15, 2001)
West Bank**



Gaza





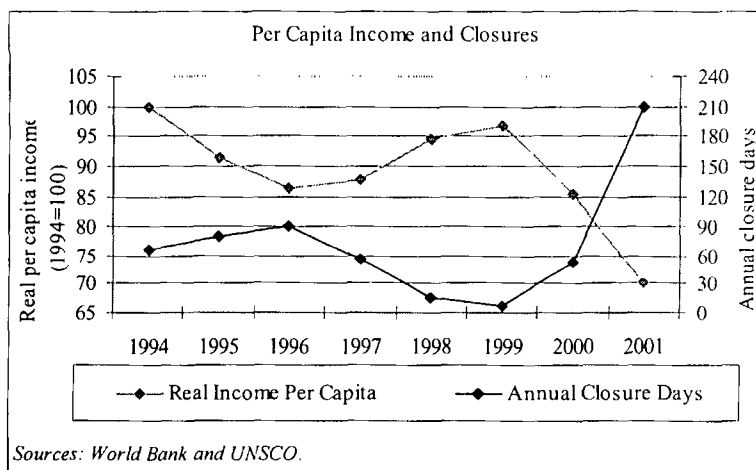
3. ECONOMIC AND SOCIAL IMPACT

ECONOMIC IMPACT

3.1 The outbreak of the *intifada* in late September 2000 fractured the dynamics of the Palestinian economic recovery of 1998-2000, and once again demonstrated the close linkage between economic growth and closure.

3.2 In the initial post-Oslo years the economy experienced rapid expansion, with the return of nationals and large inflows of public and private capital. Two years of intermittent external closures in 1995-96 precipitated a first recession. From 1998 to September 2000, closure was again infrequent, remittances from Palestinian workers in Israel fuelled demand for domestic products, transaction costs fell and private investment increased. The economy also benefited from an economic boom in Israel, which enhanced opportunities for exports of Palestinian labor and goods. For two years, the economy experienced solid economic growth and a measurable decline in poverty and unemployment. Nonetheless, this period of growth was insufficient to restore pre-Oslo per capita income levels, given the high rate of population increase in the West Bank and Gaza (over 4 percent

Figure 1: The Relationship Between Economic Growth and Closure



per annum, see Annex 1) and in the absence of significant adjustment, the prospects for sustained progress were limited. Labor supply is rapidly increasing, and the two most important sources of jobs absorption hitherto – employment in Israel and in the Palestinian Authority – are essentially saturated. Real GDP was projected by the World Bank to grow at an average annual rate of 4-5 percent, with real per capita incomes stagnant and unemployment and poverty slightly increasing. This outlook underlined the persistent vulnerability of the Palestinian economy to external shocks, particularly closure, and emphasized the importance of further structural reform measures to encourage the development of a labor-intensive, export-oriented private sector.

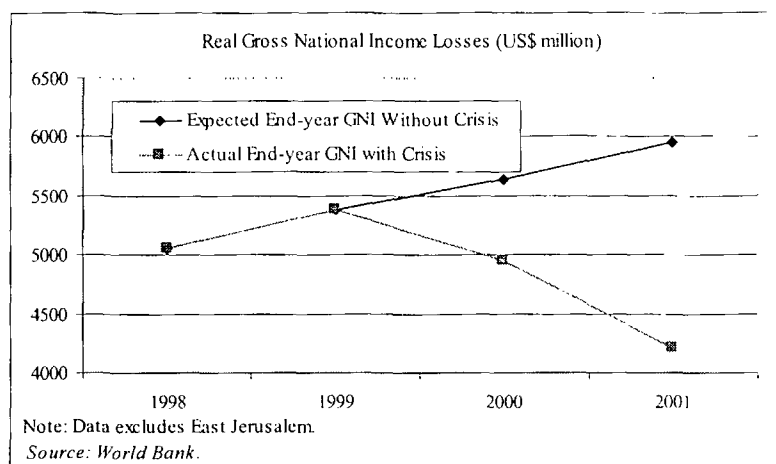
3.3 Since September 28, 2000, the situation has been characterized by unprecedented levels of confrontation and by the most severe, sustained mobility restrictions imposed on the West Bank and Gaza since 1967. Closures and confrontation have resulted in a precipitous decline in trade, employment, and investment. After sixteen months, damage to the real sector and to

investment prospects is significant. The crisis has induced a severe fiscal compression, but massive donor intervention has limited the effect of this. The private sector, in contrast, has absorbed most of the burden of the crisis. As the private sector is the engine of recovery and prosperity, this has dire implications for the future.

3.4 Available indicators suggest a sharp economic setback in the first three months of the *intifada*, followed by a slower rate of decline in 2001. The clandestine restoration of significant numbers of jobs in Israel, coping strategies adopted by households, and the efforts of the PA, donors and NGOs all helped stave off further economic collapse. In particular, donor budgetary support was used to maintain public employment and thereby a minimum level of economic demand. Relief programs, including the implementation of numerous small-scale job creation programs, also mitigated some of the hardships of the newly unemployed. Nonetheless, the numbers of the poor (defined as those with a consumption of less than US\$2 per day) rose from 600,000 in September 2000 to between 1.2 and 1.5 million by the end of 2001.

3.5 The World Bank estimates that for 2000 as a whole, real GDP declined by 6-7 percent, as a result of very poor performance in the last quarter (Q4). In 2001, real GDP declined by an additional 12 percent. The estimated decline in Gross National Income (GNI) was even larger, reaching 15 percent in 2001, as worker remittances fell by more than 40 percent compared to the low levels of 2000. Accounting for an annual population growth rate exceeding 4 percent, the decline in GNI per capita is estimated at 11.7 percent for 2000 and a further 18.7 percent for 2001.

Figure 2: Gross National Income Losses During the Intifada



3.6 More than physical damages (estimated at some US\$0.3 billion by the end of 2001, and mostly concentrated in agriculture, see paras. 3.21-3.24), economic opportunities have been lost, notably in investment (US\$1.2 billion in opportunities foregone), and in the tourism and export sectors. In total, GNI losses totaled some US\$2.4 billion in constant prices in the first fifteen months of the *intifada*. This should be compared with an estimated annual Gross National Income of US\$5.4 billion in 1999.¹⁶

3.7 This report argues that the main proximate cause of the recession is closure. It therefore follows that removing or significantly easing closure is the most important prerequisite if further decline is to be arrested and economic pressure removed from the Palestinian population. Even if

¹⁶ Palestinian Authority calculations of economic losses exceed this figure – for example, PECDAR (September 2001) estimates losses at US\$5.6 billion, Ministry of Finance (October 2001) at US\$6.9 billion and MOPIC (January 2002) at US\$7.5 billion. These estimates cover different time-frames and are derived with approaches different from those used by the Bank in the *Assessment* (see Box 4 and Annex 4).

this occurs tomorrow, World Bank projections (**Chapter 5**) indicate that it would take *at least* two years to return to a pre-crisis level of economic activity – and this assumes a healthy private sector response. It would take even longer to recover pre-crisis real per capita incomes, which are now some 30 percent lower than at the time of the Gaza-Jericho Agreement of 1994. Conversely, a sustained further tightening of closure will impoverish Palestinians and will lead to economic implosion and a scale of hardship so far only hinted at.

3.8 Nor has the *intifada* been good for the Israeli economy. The Bank of Israel (BOI) estimates that in the first three quarters of 2000 real GDP grew at 7-9 percent.¹⁷ Following the outbreak of the crisis, these trends were reversed and the annualized growth rate of real GDP in the last quarter turned sharply negative. In the subsequent quarters, growth has remained subdued although some recovery has taken place. On January 13, 2002, BOI reported that the *intifada* had cost Israel some 13 billion Shekels, or 4 percent of GDP.¹⁸

3.9 In a forecast made prior to the global turndown following the September 11 terrorist attack on the US, the Israeli Ministry of Finance projected that real GDP would grow less than 1 percent in 2001 but would rebound to approximately 4 percent in 2002, even assuming that the crisis remained unresolved. Nonetheless, this represents a flattening of Israel’s medium-term growth prospects, with particular effects on tourism (a fall in average numbers of monthly visitors by a half comparing *pre-intifada* 2000 with the present), and in construction (where approximately one-third of the total workforce has until recently been Palestinian).

Figure 3: Real GDP Growth in Israel, 1996-2001



Employment

3.10 The impact of the crisis has been felt very largely in the private sector, and is experienced through loss of jobs and a loss of earnings as a direct or indirect result of closure. The labor force in WBG (excluding East Jerusalem) was some 688,000 strong on the eve of the *intifada*.¹⁹ Formal employment statistics²⁰ indicate that unemployment increased from 10 percent in

¹⁷ Bank of Israel. Quarter on quarter, annualized growth rates, seasonal adjusted data.

¹⁸ “According to the bank, the overall production losses are actually higher, because in addition to the direct losses sustained as a result of the violence, there have also been indirect losses, in the form of a reduction in private consumption and a drop in investments, which can be attributed to a decrease in private income.” Moti Bassok, Ha’aretz Correspondent, 1/13/2002.

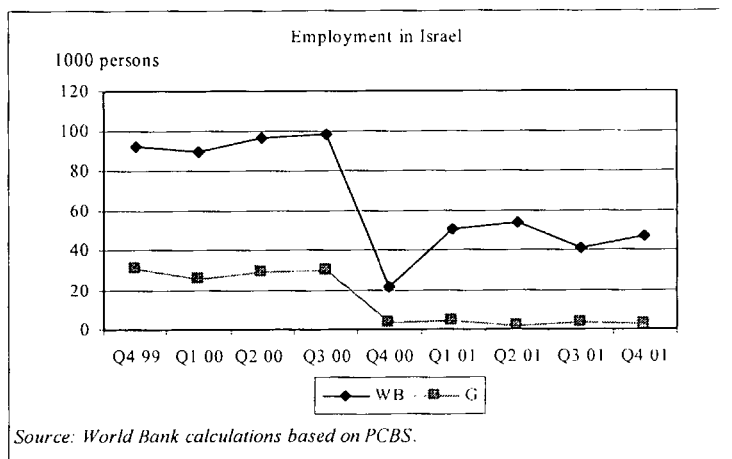
¹⁹ Includes employment in Israel and the settlements as well as those considered underemployed; excludes “discouraged workers” not actively seeking employment. Source: Palestinian Central Bureau of Statistics (PCBS) and World Bank staff estimates.

²⁰ Palestinian Central Bureau of Statistics (PCBS).

Q3/2000 to 26 percent in Q4/2001, after peaking at 28 percent in December 2000.²¹ These numbers require qualification, however. For one thing, the labor force decreased during this period as a growing number of people of working age were discouraged from seeking jobs by movement restrictions, depressed demand for jobs and falling wages. Accounting for the number of workers discouraged from seeking work since the beginning of the *intifada* raises unemployment to 35 percent by end-December 2001, as compared to 20 percent one year before. Another way to illustrate this is to compare the number of jobs to the total population. In September 2000, 1 out of 4.8 Palestinians had a job; in December 2001, 1 out of 6.5 Palestinians had a job. Nor do these figures speak to underemployment or the income derived from these jobs, many of which were intermittent in nature and paid less than previous employment.²²

3.11 Direct impact of closure – the loss of jobs in Israel. Immediately following September 28, 2000, the number of Palestinians working in Israel plummeted. During the last quarter of 2000, some 100,000 jobs of a total of 125-130,000²³ evaporated. This was in part due to a dramatic reduction in the number of permits provided,²⁴ in addition, controls on routes to Israel and the settlements were significantly tightened, which discouraged the large number of clandestine (non-permit holding) workers. These clandestine workers accounted for more than half the total number of Palestinians working in Israel and the settlements. It is also likely that the demand for Palestinian workers by Israeli firms decreased in light of security concerns. Employment recovered somewhat in 2001, with an estimated average of approximately 50,000 Palestinian workers commuting to Israel daily from the West Bank, albeit subject to sudden and sharp closures. Nonetheless, the number of Palestinians working in Israel is at best less than half of pre-crisis levels, and almost none of them are from Gaza.

Figure 4: Palestinian Employment in Israel, 1999-2001



²¹ The Palestinian workforce totaled some 734,000 workers in September 2000, including East Jerusalem (source: PCBS labor surveys). See World Bank, *West Bank and Gaza Update*, June 2001, for a general discussion of the different definitions and measures of unemployment rates.

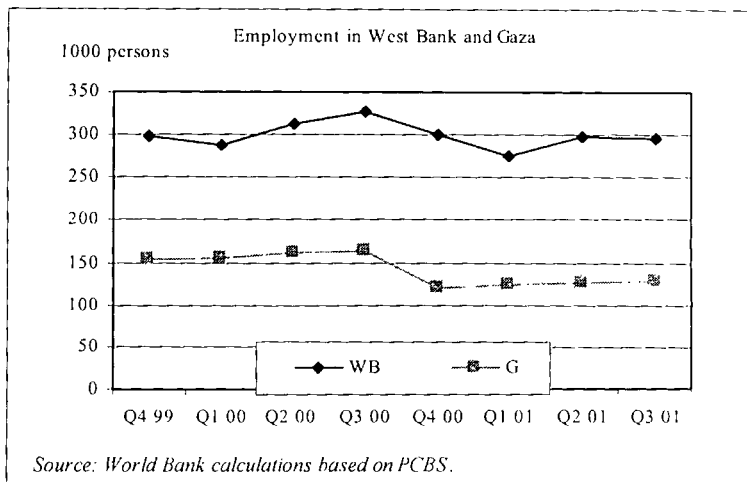
²² The ILO definition of employment used by PCBS stipulates that all persons aged 15 or more who were working at a paid job for at least one hour during the reference week, or who did not work but held a job or owned a business from which they were temporarily absent, are considered employed. Under this definition, underemployment is said to exist when a person's work is not compatible with his/her occupational skills.

²³ Data excludes East Jerusalem.

²⁴ According to data collected by UNSCO the average number of permits issued during the last quarter of 2000 was 8,500, compared to an average level of approximately 55,000 prior to the crisis.

3.12 **Indirect impact of closure – the loss of jobs in WBG.** Employment in Israel is of great importance to Palestinian living standards, as the wages of Palestinian workers in Israel are significantly higher than in the West Bank and Gaza.²⁵ The drop in worker remittances inevitably depressed demand for Palestinian goods within WBG. This effect, coupled with the growing difficulty of conducting business, also led to reduced labor demand internally. Gaza experienced a fall in domestic employment of more than 25 percent during the first quarter of the crisis, reducing the number of employed from 164,000 to 120,000, reflecting both the importance of worker remittances from Israel in the Gaza economy and the isolation of Gaza following the outbreak of the crisis. In 2001, the situation improved slightly, due in part to donor-financed employment schemes. In the West Bank, the level of domestic employment declined more gradually over the first six months of the *intifada*, and then started to rebound afterwards. Still, the total number of (public and private) jobs in West Bank and Gaza by the end of 2001 was approximately 60,000 lower than before the crisis, while during the same time the working age population increased by more than 100,000.

Figure 5: Palestinian Employment in WBG, 1999-2001



Trade

3.13 The flow of goods and services traded with Israel and the rest of the world has been significantly affected. In the table below, trade figures are estimated from three sources: from the Israeli Central Bureau of Statistics (ICBS), from records of truckload movements, and from clearance revenues (VAT and import duties).²⁶

²⁵ Using 1998-99 figures, Ruppert Bulmer (World Bank, 2001) estimates that for workers with similar individual characteristics (education, age, sector, etc.), commuting to Israel added a 91 percent premium to wages when compared to working in the West Bank and Gaza.

²⁶ The three indicators are not directly comparable: estimates from the ICBS cover goods and services traded between Israel and West Bank and Gaza, but do not cover Palestinian trade with the rest of the world. Estimates based on truckload movements do not cover services, and do not capture the value of traded goods. Estimates based on VAT clearances only capture trade between the West Bank and Gaza and Israel, and exclude trade in agricultural goods (which are exempted from VAT). In addition, none of the three indicators capture clandestine trade between Israel and the West Bank, which is significant because of the porosity of the border. Nor are these three indicators strictly comparable in time: for instance, truckload movements are not necessarily registered at the same time as VAT declarations.

**Table 1: Measures of West Bank & Gaza Trade 2000-2001
(US\$ million)**

Measures	Q1-00	Q2-00	Q3-00	Q4-00	Q1-01
ICBS-exports (US\$ mil.)	111	116	118	93	64
ICBS-imports (US\$ mil.)	454	500	563	299	222
Exports – VAT based (US\$ mil.)	119	126	114	96	114
Imports VAT Based (US\$ mil.)	447	483	493	306	285
Exports - Truckload movements	2,387	2,127	1,650	701	1,805
Imports - Truckload movements	11,542	13,264	13,704	3,378	5,728

Sources: ICBS, UNSCO, Ministry of Finance.

3.14 ICBS information suggests that the relative decline in imports from Israel since October 2000 was larger than the decline in exports of Palestinian goods to Israel. During the first three quarters of 2000 imports grew more rapidly than exports, then fell dramatically with the *intifada*. Exports did not fluctuate as much. This estimate is substantiated by the records of truckload movements and estimates of trade flows based on VAT declarations, and could be explained by several factors – higher transaction costs for imports than exports, the substitution of cheaper domestic goods for Israeli imports, and lower overall domestic demand (while the demand for Palestinian goods in Israel and elsewhere remained relatively unaffected).

3.15 In absolute terms, though, both import and export volumes decreased; this inevitably had negative effects on the efficiency of the Palestinian productive system, which is highly dependent on imported inputs, as well as on the welfare of Palestinian consumers and on the potential tax revenue of the PA. Exports of agricultural goods are estimated by the World Bank to have been particularly affected by the crisis, with losses equivalent to 30 percent of their export potential in 2001. Manufacturing exports lost some 24 percent of their potential export value.

Investment and Productive Capacity

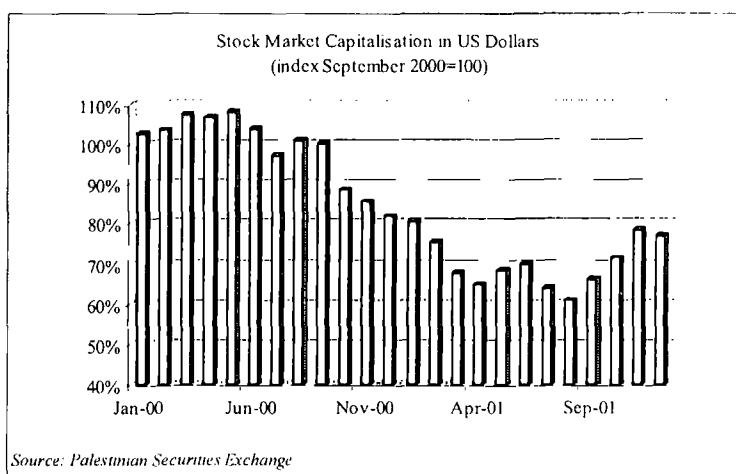
3.16 **Private Investment.** High risks and low returns have inevitably led to decreased investment and a withdrawal of capital from the market. On the risk side, the fear of damage from fighting, inability to meet export orders on time, the erratic availability of imports and the reduced capacity of the Palestinian Authority to enforce property rights have all loomed large in the minds of potential investors and banks; in addition, returns have been depressed by low domestic demand and increased transaction costs. Potential investment has been further eroded by the diversion of working capital to maintaining firms in the face of losses, as well as to sustaining household consumption. Investment in sectors which offered opportunities before the crisis, such as tourism, housing, or export-oriented activities (notably within the framework of the new industrial estates) were particularly hard-hit. Tourism projects were rapidly mothballed as tourists abandoned conflict-ridden areas such as Bethlehem. Construction investment (both for residential housing and private business) has been hamstrung by the impact of closure on the flow of materials, above all cement. Serious confrontations near the Gaza and Jenin Industrial Estates have discouraged further investment and led some firms to disengage.

3.17 **Public Investment.** Prior to the crisis, some 93 percent of public investment was financed by donors (2000), through grants or soft loans. The increased difficulty of conducting

business has significantly reduced the pace of disbursement by donors on public infrastructure; while the overall donor response has been generous and appropriate, it embodies a cost in investments foregone in favor of consumption (emergency) contributions (para. 3.28). PA contributions to public investment in 2001 actually increased from US\$15 million in 2000 to US\$21 million in 2001, but remain marginal. Based on PA data, it is estimated that total public investment fell by approximately 17 percent in 2000 compared with 1999, and by a further 25 percent in 2001.

3.18 Lost Investment. The lack of national accounts does not allow regular monitoring of investment expenditures, particularly private investment expenditures. However, some indirect indicators can be used to review the impact of the crisis on investments. One such is the volume of imported cement, since cement accounts for some 80 percent of construction costs. According to UNSCO, cement imports dropped by 64 percent between the 3rd and 4th quarters of 2000. Another indicator is the number of new company registrations, which fell by 80 percent during the same period.²⁷ The Palestinian Monetary Authority²⁸ reports that bank credit to the private sector (to individuals and businesses, including for credit facilities and brokers’ bills and discounted items) fell 14 percent, from US\$1,064 million in September 2000, to US\$911 million in December 2000. In 2001, bank credit to the private sector continued to decline, albeit at a lower pace. In November 2001, it still amounted to US\$862 million. A further measure is market capitalization. Between September 2000 and December 2001 the capitalization in US dollars of firms registered on the Palestinian stock exchange dropped by one fourth,²⁹ overall private sector market capitalization is estimated by the Center for Private Sector Development (CPSD) to have dropped by up to 40 percent during the past year.³⁰

Figure 6: Palestinian Stock Market Capitalization



3.19 All in all, the World Bank estimates that total investment may have decreased by 19 percent in real terms in 2000, and by a further 30 percent in 2001.

²⁷ Some caution is needed here, as a proportion of the previous registrations were “virtual” in the sense that they have not resulted in actual business activity.

²⁸ *PMA Statistical Bulletin, Issue 38, September 2001.*

²⁹ According to the Palestine Stock Exchange website, stock market capitalization fell by 23 percent between September 2000 and December 2001, from US\$936 million to US\$722 million, with a dip of US\$622 million in September 2001.

³⁰ *The State of Private Sector, 2001* – a survey by CPSD of 518 private firms, of which one third are industrial, one third agricultural, and one third in trade and services.

3.20 Physical Damage. The Palestinian Authority has made a number of estimates of the physical damage caused by closure and armed confrontation; these are summarized in **Annex 3**. These estimates vary depending on assumptions, methodology, time-frames and the availability of data. Drawing on these estimates, the Bank conducted its own assessment of damage inflicted between October 2000 and June 2001. This initial work was then updated to reflect additional damage between July and the end of December 2001. Further details and earlier estimates are provided in **Annex 3**.

Box 4: The Measurement of Damages

It is important to distinguish between losses in capital stock, and losses in revenue flows.

Capital stock. Confrontation and closures have damaged and/or accelerated the rate of depreciation of productive capital stock (damaged buildings, uprooted trees, road and soil degradation, etc.). One option when valuing capital stock losses is to measure the cost of replacement. For some items market replacement costs are available. For others (e.g. historical buildings or unique natural endowment), where there is no possibility of replacement, price estimation is much more speculative. A second option is to value revenue foregone as a result of the capital loss. This is a very complex task, and relies on a forecasted stream of future revenue had the capital stock not been damaged. Productive assets depreciate slowly, so this method involves assumptions about economic, social, political and technological trends over many years. Measuring these revenue streams in present values then requires further assumptions about actualization rates, or the degree of preference given to the present, in comparison to the future. The World Bank approached *capital stock losses* by using the replacement cost approach. Building damage was estimated at reconstruction costs, plus a conservative average rate of 20 percent to account for furniture and equipment losses – but without any attempt to estimate losses of inventory or supplies (which was judged too difficult). Estimates of damage to roads included base course and resurfacing repair required by armored vehicle passage, ripping and excavation, as well as from the closure-induced over-trafficking of secondary roads. Estimates of damage to agricultural capital involved valuing the replacement cost of uprooted trees, as well as of displaced topsoil and destroyed wells, greenhouses and irrigation systems. Since a replacement fruit-bearing tree cannot yield for a number of years, the lost income associated with this biologically-determined period was factored in (thus the replacement cost of an olive tree is estimated at US\$250, including seven years of lost/reduced produce). The period of estimation covered October 2000 – end June 2001.

Revenue flows. Losses in revenues result from depressed prices, reduced productivity and a reduced stock of productive resources. Measurement is difficult as this means estimating what revenues would have been in the absence of crisis, as well as of macro-economic forces at play during a crisis. The most consistent and simplest estimate of revenue losses in a defined period is probably obtained by comparing the difference between actual Gross National Income (GNI) and presumed GNI had there been no crisis. This method avoids double accounting and also covers all types of economic losses in a given period. On the contrary, adding capital losses and revenue losses mix stocks with flows, incorrectly combining two alternative definitions of economic loss. The World Bank used with/without crisis GNI comparisons to estimate Palestinian *revenue losses*.

3.21 The Bank assesses total damage in WBG as of the end December 2001 at about US\$305 million, almost twice the earlier estimate for the October 2000 -- June 2001 period (US\$168 million).³¹ Gaza suffered most, sustaining about two-thirds (US\$193 million) of total WBG damage, most acutely in the Gaza City and North Gaza governorates (30 and 25 percent of

³¹ It should be noted that the June figure is a re-calculation. The Bank originally estimated total damage in WBG as of the end of June 2001 at approximately US\$118 million. This compares quite reasonably well with estimates by the President's Office of about US\$116 million (which excludes security buildings). However, neither estimate fully captured the replacement cost in agriculture, in particular on account of damage to topsoil and trees. The current estimate does.

Gaza damage). In the West Bank, the Ramallah and Bethlehem governorates suffered the most, with some 22 and 19 percent respectively of the West Bank damage total.³²

Table 2: Physical Damage between September 28, 2000 and December 31, 2001

<i>Sector</i>	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>
	US\$ million			Percent		
1. Infrastructure	12.7	27.4	40.1	7%	24%	13%
2. Agriculture	141.3	35.3	176.6	73%	31%	58%
3. Public Buildings	16.7	24.1	40.8	9%	21%	13%
4. Private Buildings	22	25.6	47.5	11%	23%	16%
Total	192.7	112.4	305.1	100%	100%	100%

3.22 Sectorally, *agriculture* sustained the highest overall damage -- about US\$177 million or almost 60 percent of the WBG total (but a relative reduction since June 2001). Damage to agriculture was much higher in Gaza than in the West Bank (73 percent versus 31 percent of the regional totals). Damage to agriculture in Gaza accounted for 89, 84, 76 and 72 percent respectively of the total damage in the North, Middle, Khan Younis and Gaza City governorates. In the West Bank, agricultural damage was highest in Qalqilia, Jericho and Salfit where it represented, respectively, 80, 69 and 67 percent of total damage. Agricultural damage was lowest in the Hebron, Tulkarem and Jerusalem governorates (6-7 percent of the governorate totals).

3.23 Next most severe was damage to *Private Buildings*, which sustained about US\$48 million or 16 percent of total damage. In this sector, destruction was higher in the West Bank than in Gaza, US\$25 million as opposed to US\$22 million. While small in absolute terms, this represents a significant relative difference in the respective regional totals (23 percent versus 11 percent). Within Gaza, the Gaza City governorate bore the brunt of the damage, 47 percent of the sectoral total, followed by the Rafah, Middle and Khan Younis governorates with 20, 16 and 11 percent of the sectoral total respectively. Within the West Bank, the Bethlehem and Hebron governorates suffered most, accounting for 46 and 28 percent of the sectoral total. The *Residential Buildings* subcategory of the sector dominated this type of damage, accounting for about US\$32 million in all. When it comes to damage to *Private Commercial and Industrial Buildings*, the lion's share in the Gaza region was sustained in the Gaza City governorate (some 90 percent of the subsector). In the West Bank, three governorates (Bethlehem, Hebron and Qalqilia) accounted for almost 70 percent of the subsectoral total. Damage to *Tourism Buildings* was significant in the West Bank, where it accounted for 4 percent of total West Bank damage -- essentially in Bethlehem, with almost 80 percent of the subsectoral total.

3.24 *Infrastructure* and *Public Buildings* ranked about equal in terms of overall damage sustained, at 13 percent of the WBG total. In the period since June 2001 the share of this sector in the total increased significantly (from about 8 percent each). In respect of *Infrastructure*, Gaza

³² This represent a significant change in the distribution of damage in WBG since June 2001, and reflects a shift in the focus of hostilities in the latter period. At end June 2001, the Gaza City governorate accounted for 24 percent of the Gaza total while the North Gaza governorate accounted for 29 percent. By the end of 2001 the total damage in Gaza City had overtaken damage in the North Gaza governorate. In June, Qalqilia governorate had sustained the most damage in the West Bank, with 23 percent of the regional total, while Ramallah governorate had suffered 22 percent, Tulkaren 15 percent and Bethlehem 14 percent of the West Bank total.

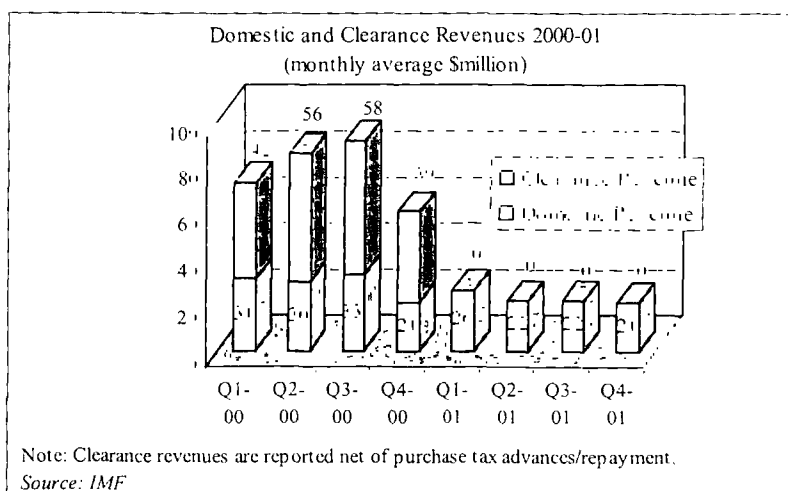
suffered much less in relative terms, with the sector suffering 7 percent of total damage (versus 24 percent in the West Bank). In both Gaza and the West Bank, roads dominated (largely due to over-trafficking). Within the *Public Buildings* sector, Gaza suffered less than the West Bank with 9 versus 21 percent of the regional totals; in both regions, though, there was a significant increase in damage sustained in the June-December 2001 period. Damage to major public buildings such as the Gaza Airport and the national television facilities in the West Bank feature prominently here. Finally, there has been a significant increase in the damage to security related buildings in recent months, once again reflecting a change in the pattern of hostilities since June 2001.

3.25 Although significant, the total amount of physical damage does not compare to the loss in investment flows resulting from reduced savings and fewer viable business opportunities. The Bank estimates that cumulative lost investment opportunities reached US\$1.2 billion by the end of 2001.

Fiscal Accounts³³

3.26 **Central Government Revenue.** PA current revenues are intimately linked with the level of Palestinian demand, with approximately 80 percent of total current revenues derived from indirect taxes on consumption -- notably VAT, import taxes and excise on fuel and tobacco. In addition to the severe impact on PA revenue of rising unemployment and reduced demand, Israel has since December 2000 declined to transfer to the PA those funds which are collected by the Israeli Tax Administration but which accrue to the PA through the revenue clearance system; as of end-December 2001, these withholdings had reached NIS 2.1 billion -- or approximately US\$507 million if the NIS amount is converted each month at the prevailing average NIS/US\$ exchange rate of that month,³⁴ and continue to accumulate at approximately US\$29 million per month. In addition, mobility restrictions led to a loss of efficiency in domestic tax collection. As a result, revenues fell from a monthly average of \$91 million in Q3/2000 to \$22 by Q3/2001 (a loss of 76 percent between the periods).

Figure 7: The Revenues of the Palestinian Authority, 2000-2001



³³ See also **Annex 2** [IMF].

³⁴ Net of certain unpaid PA bills. In January 2002, the Minister of Finance wrote to his Israeli counterpart proposing that Israel deduct from the clearance revenues owed some NIS 79 million on account of electricity bills, medical expenditures and animal vaccines. GOI has accepted the offer of NIS 70 million for electricity payments.

Box 5: The Revenue Clearance System

The Paris Protocol signed in 1994 by the Government of Israel and the Palestinian Authority defines the rules and arrangements regarding the apportioning of indirect taxes (mainly VAT, purchase taxes and import duties) collected within Israel and the West Bank and Gaza by the Israeli and Palestinian administrations. The clearance of tax receipts between Israel and WBG is made according to the “destination principle”, i.e. where the item will finally be consumed. Thus taxes levied by the Israeli fiscal administration at an Israeli port on a product imported from abroad and destined for WBG will in time be transferred to the PA. A Palestinian producer using an Israeli intermediate input in his production process will purchase at a price including VAT paid in Israel, and will present the invoice to the PA. In turn, the PA will claim reimbursement of this VAT from the Government of Israel and will remit it to the Palestinian producer.

In addition to indirect taxes, which represent the bulk of clearance revenue for the PA, the Paris protocol specifies that 75 percent of the income taxes and 100 percent of the health fees paid by Palestinian workers in Israel are to be transferred to the PA.

Before December 2000, the Israeli and Palestinian Ministries of Finance met every month to reconcile their accounts and agree on the net amount to be transferred to the PA. As a net importer of Israeli goods, transfers from the clearance revenue system have been the most important source of revenue for the PA – more than 60 percent of its total revenue (not including foreign assistance) from 1995 to 2000, and reaching an average of \$58 million per month in Q3/2000.

3.27 This collapse in central government revenue was partly compensated by emergency budget support, of which the PA received US\$584 million between November 2000 and December 2001. This consisted of \$405 million from Arab League states through the Islamic Development Bank (IDB),³⁵ \$114 million from the European Union, US\$40 million from Saudi Arabia, US\$15 million from the UAE and US\$10 million from Norway, an average of US\$48.7 million per month (or 54 percent of monthly budget outlays). With domestic revenues averaging US\$22.75 million per month in 2001, this left an unfunded average budget gap of approximately US\$19.6 million (21 percent of outlays), which has been managed through a combination of accumulating arrears to suppliers, taking occasional loans from domestic banks,³⁶ trimming operating budgets and delaying the payment of certain non-salary expenses (e.g. to social hardship cases and to the Gaza Pension Fund).

3.28 **Central Government Expenditure.** Total expenditures were reduced from a monthly average of US\$107 million during the third quarter of 2000 to an average of \$90 million from the second quarter of 2001 to the present. This reduction in expenditures fell almost entirely on the non-salary operating cost component of the budget; indeed, the monthly salary bill, which has been paid each month,³⁷ increased from around US\$53 million prior to the *intifada* to US\$58 million by the end of 2001, while the number of civil servants on the payroll rose by almost 10,000 during the same period. A considerable portion of the available non-wage expenditures were dedicated to emergency expenditures, mostly in the social sectors; these averaged US\$13 million per month in 2001 (about 73 percent of non-wage recurrent spending),

³⁵ In February/March 2001, interest-free loans of US\$240 million were committed through the IDB, and this was followed by a further commitment of US\$165 million in July 2001.

³⁶ Credit to the commercial banking system stood at approximately US\$300 million by the end of 2001, and should not be increased. Commercial banks are still prepared to extend “exceptional loans” to the PA in instances where external budgetary resources are available to underwrite them. Thus in January 2002 the Arab Bank extended a US\$45 million bridge loan to the PA in anticipation of US\$45 million from the Saudi Fund in three tranches between January and March.

³⁷ See Chapter 5 for an account of the current liquidity crisis facing the PA.

but declined progressively from US\$19 million in the first quarter 2001 to US\$8 million in the last quarter of the year. These emergency expenditures left little for traditional (non-emergency) non-wage expenditures, and it is estimated that the latter declined from some \$54 million to \$14 million per month when comparing the third quarter of 2000 with the fourth quarter of 2001.

Table 3: PA Fiscal Accounts - Monthly Average (US\$ million)

	2000 Q1	2000 Q2	2000 Q3	2000 Q4	2001 Q1	2001 Q2	2001 Q3	2001 Q4
Revenue	72	102	88	49	26	22	22	21
Domestic	31	30	33	21	26	22	22	21
Clearance	42	72	55	28	0	0	0	0
Of which: purchase tax advances/repayments	0	16	-3	-11	-3	0	0	0
Current expenditure 1/	82	103	107	105	94	90	90	90
Wages	47	51	53	55	55	57	57	58
Non-wages	35	52	54	50	38	34	33	33
PA-financed capital expenditure	0	2	1	2	1	1	2	3
Recurrent balance including PA-financed capital expenditure	-10	-3	-19	-58	-68	-70	-70	-72
Financing	10	3	19	58	68	70	70	72
Expenditure arrears (net accumulation)	1	1	19	1	31	19	20	22
External budgetary financing	0	0	0	18	26	48	49	54
Domestic bank financing and residual	9	2	0	39	11	4	1	-3
Memorandum items:								
Stock of expenditure arrears (end of period)	93	155	250	305	365	430
PA employment (in thousand employees, end of period)	107.2	...	112.7	114.9	117.1	118.8	119.0	122.1

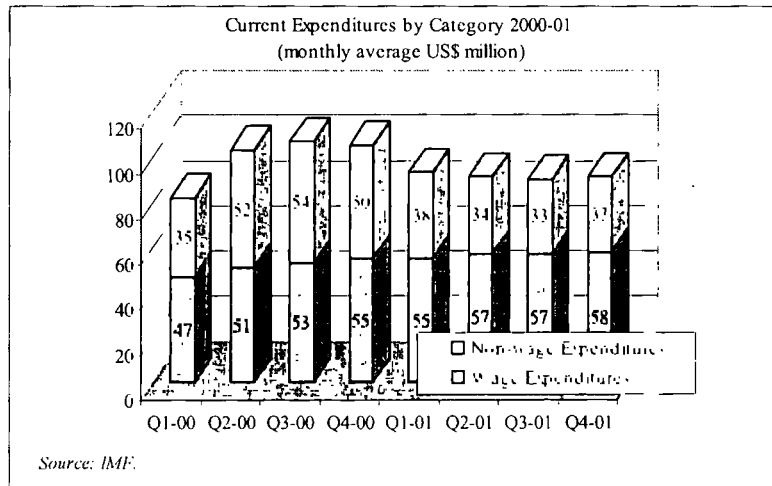
1/ All expenditure components are presented on a commitment basis, unless otherwise noted.

Sources: Palestinian Authority (PA); and IMF staff estimates and projections.

3.29 Inconsistent information on expenditures across ministries prevents a comprehensive analysis of the fiscal situation by sector and a full identification of gaps. Nevertheless, the experience of specific ministries illustrates the nature of the difficulty faced in maintaining the delivery of basic services to the public. The Ministry of Health's operational expenditures were cut drastically in 2001: the Ministry received \$34.5 million from the PA and donors in 2000; by midyear 2001, only US\$9.5 million had been received for an expanded program.³⁸ Actual budgets transferred have often been far less. This issue is further discussed in **Chapter 4**.

³⁸ MOH data.

Figure 8: The Composition of PA Expenditures, 2000-2001



3.30 **Local Government Finance.** Municipal finances have been severely stretched by the crisis, and unlike those of the PA, have not thus far benefited from external budget support. In aggregate terms the annual recurrent budget of all 140 municipalities in 2000 amounted to some \$130 million, or about 11 percent of the PA’s budget for 2000. No complete data exists on the overall fiscal situation of these municipalities, but based on the survey conducted by the Bank for the *Assessment*, municipalities in mid-late 2000 appeared to be facing a monthly deficit of some 10-15 percent of their (reduced) budgets. Under such circumstances services have begun to break down.

3.31 The situation in each municipality obviously differs, depending on the structural nature of the local economy and on the local impact of the crisis. Some common developments can be observed, looking at the experience of a sample of large and small municipalities (Tables 4 and 5).

3.32 *Revenues.* Municipal revenues accrue from three sources – transfers from the PA (*ad hoc*, often in the form of netting out of unpaid utility bills owed Israeli companies through the revenue clearance process), local taxes (especially building and professional licenses), and user charges on water and electricity. On average in the 14 municipalities sampled, quarterly revenues were 29 percent lower at end-June 2001 than at end-June 2000, and 30 percent lower compared to the situation at end-September 2000. Revenues were particularly hard-hit during the last quarter of 2000, but recovered somewhat during the first six months of 2001.³⁹ The decline in revenues resulted mainly from an increasing inability by families to pay their utility bills. Tax receipts also declined as a result of depressed economic activity.

³⁹ It is notable that revenues in many municipalities samples rose in the first quarter of 2001 (Table 4). This is explained by the fact that most market fees, shop license fees and trade permit fees are collected at the beginning of each calendar year.

**Table 4: Revenues in 14 Sample Municipalities, 2000-2001
(quarterly average, US\$ million)**

	<i>Q2-2000</i>	<i>Q3-2000</i>	<i>Q4-2000</i>	<i>Q1-2001</i>	<i>Q2 2001</i>
Gaza City	13.4	12.1	10.4	9.4	12.6
Rafah	2.8	2.4	1.4	1.5	1.4
Khan Yunis	2.9	4.2	1.5	3.0	1.8
Beit Hanoun	0.8	1.0	0.4	0.4	0.4
Ramallah	3.7	4.5	2.2	6.8	2.7
Al Bireh	6.3	3.4	5.7	5.8	2.7
Jenin	8.5	8.8	5.2	10.2	7.3
Bethlehem	2.2	1.8	1.1	2.9	1.4
Jericho	2.9	3.2	1.1	2.1	1.6
Nablus	45.8	49.2	36.3	39.7	41.4
Hebron	27.8	29.0	14.9	28.1	21.8
Qalqilya	6.30	9.71	4.66	5.08	4.36
Doura	2.02	1.91	1.56	1.78	2.05
Anabta	0.94	1.04	0.79	0.76	0.73

Source: World Bank.

3.33 *Expenditures.* As a consequence, most sampled municipalities had no choice but to reduce expenditures, by an average of 20 percent in Q3/2001 as compared with Q3/2000. Cuts again fell mainly on municipal services (most notably garbage collection), as well as on provisions for capital investment.

**Table 5: Expenditures in 14 Sample Municipalities, 2000-2001
(quarterly average, US\$ million)**

	<i>Q2-2000</i>	<i>Q3-2000</i>	<i>Q4-2000</i>	<i>Q1-2001</i>	<i>Q2-2001</i>
Gaza City	16.0	16.3	12.9	10.6	10.5
Rafah	2.5	2.6	2.1	1.3	1.8
Khan Yunis	3.0	3.8	2.6	2.7	2.3
Beit Hanoun	0.6	0.9	0.7	0.5	0.5
Ramallah	4.9	4.1	4.0	4.0	3.5
Al Bireh	3.2	4.0	3.0	3.2	2.4
Jenin	7.7	9.7	8.1	6.9	8.0
Bethlehem	3.0	1.7	2.0	2.1	2.0
Jericho	3.1	4.0	2.6	2.2	2.4
Nablus	30.1	58.1	38.9	35.3	50.1
Hebron	24.3	21.9	14.1	23.6	22.0
Qalqilya	4.54	6.23	6.89	4.44	4.04
Doura	1.74	1.87	1.38	1.48	2.25
Anabta	0.80	0.82	0.55	0.71	0.75

Source: World Bank.

3.34 With expenditures falling less than revenues, budget deficits rose, and the sampled municipalities on average ran deficits of about 10 percent of expenditures. These deficits were financed by withholding staff salaries and non-payment of suppliers – in particular, Israeli suppliers of electricity. Over the period of a year, the total stock of liabilities of the sampled

municipalities went from less than US\$1 million to more than US\$4 million. Extrapolating for all municipalities (on the assumption that the sample is fairly representative), the national stock of municipal debt probably reached US\$20-23 million by the end of December 2001, and is increasing at a monthly rate of about US\$1 million.

Box 6: The Palestinian Local Government System

The dominant entities in the Palestinian local government system are the *municipalities*, which have well-established service delivery and regulatory functions (including the provision of electricity, water supply and sanitation services, solid waste management, local road construction and maintenances, libraries, parks and recreation facility management, fire abatement, slaughter-house management, market supervision, land use planning and development, building approvals, and business and professional licensing). *Village councils*, which in some cases have populations and areas that compare to those of the municipalities, are the next level of local government. They feature a representative government structure but lack the broad range of statutory functions and revenue raising options associated with municipalities. *Villages* without councils are the most numerous type of local government unit. They are administered by appointed mukhtars.

Since September 1997, local governments have come under one common legal system. The Local Administration Act is based on strong central controls, and extensive discretion to manage the local government system is vested in the Minister of Local Government. The Law includes a number of potential benefits. For instance, it allows the Minister of Local Government to strengthen the role of village councils and the representation of the people at the village level by replacing mukhtars with elected local committees, and it permits him to upgrade these local committees to village councils, and village councils to municipalities.

Before the *intifada*, the coverage, reliability and quality of most local government services were considered less satisfactory than those provided in countries of similar per capita incomes. Municipalities were unable to respond to service demands adequately, for a variety of reasons that included limited managerial capacity (which resulted in low revenues and excessive expenditures), and inadequate provisions for the operation and maintenance of existing assets.

According to the World Bank, the origins of many local government problems lie in the structure of municipal finances, and the nature of the intergovernmental fiscal system. The income and expenditure profile of most municipalities in the West Bank is dominated by electricity and water services, and cash surpluses from these utilities fund the deficits in other municipal operations. The current system has two major disadvantages, though: first, services are atomized, which strongly limits potential economies of scale and complicates distribution; second, there are no provisions for transfers from rich municipalities/villages to poorer ones. In addition to the revenues from utilities, municipalities are supposed to receive a portion of the taxes collected by the central government on their behalf (gas taxes, vehicle registration charges and, for the West Bank, property taxes). Thus far these taxes have been a source of conflict between central and local governments, and have often been withheld by the former

Source: "West Bank and Gaza, Intergovernmental and Municipal Finance", November 2000, The World Bank, Washington D.C.

3.35 **Arrears.** The national stock of arrears (PA and municipalities) has increased dramatically and is estimated to amount to some US\$450 million by the end of 2001, with US\$430 million of these central government arrears. (The extent and composition of PA arrears is currently under review by the Ministry of Finance and IMF and still needs to be confirmed.) The arrears consist mainly of credit to private sector suppliers, and include unpaid PA pension contributions and seriously delayed payments to families on social welfare.⁴⁰ This compares with a stock of US\$155 million in Central Government arrears at the end of December 2000. In other words, US\$22.5 million of arrears have on average accumulated each month during the *intifada*. This level of arrears accumulation has had a pernicious impact on the private sector, resulting in an

⁴⁰ Some 43,000 hardship families are currently seven months behind on payments owed, and are receiving a payment in only one month out of every three.

acute liquidity shortage, mounting non-performing loans in the banking system, and increasing cases of insolvency. Vendors have felt compelled to continue providing credit, but many have now reached a point where they are no longer willing, or able, to do so. Settling these arrears will be a matter of top priority once Israel remits the withheld clearance revenue (NIS 2.1 billion – or approximately US\$0.5 billion in gross terms owed as of end-December 2001).

Output

3.36 GNI and GDP. Gross National Income sums Gross Domestic Product and factor revenue from abroad. GNI declined more rapidly than GDP, as wage incomes of Palestinian workers in Israel were relatively more affected than domestic activity. Real GNI fell by approximately 8 percent in 2000; real GNI per capita fell by about 12 percent in 2000 and by a further 19 percent in 2001.

Figure 9: Palestinian Arrears, 1999-2001

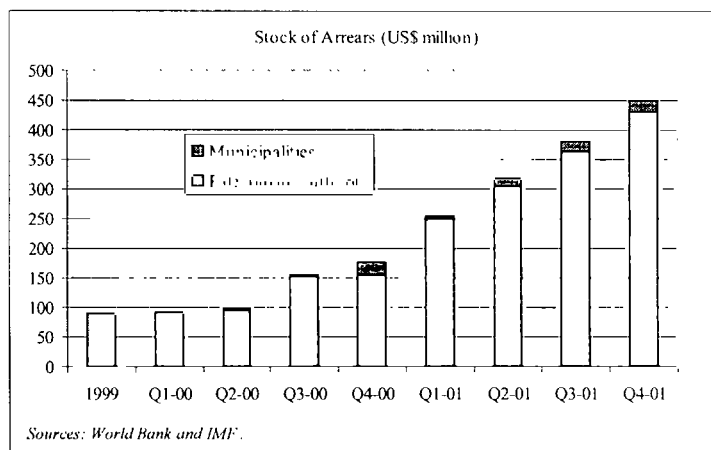


Table 6: A Summary of West Bank and Gaza Macroeconomic Trends, 1997-2001⁴¹

	1997	1998	1999	2000	2001
Gross National Income (GNI), US\$ m.	4,565	5,058	5,086	5,089	4,609
Gross Domestic Product (GDP), US\$ m.	3,959	4,230	4,288	4,360	4,093
Real annual change					
GNI per capita	1.8%	7.7%	2.2%	-11.7%	-18.7%
GDP per capita	-1.1%	3.9%	3.0%	-10.3%	-15.7%
Private Consumption	4.0%	9.0%	6.1%	-6.7%	-14.0%
Public Consumption	10.0%	7.0%	9.7%	15.5%	-5.0%
Total Fixed Investment	7.7%	8.4%	16.1%	-19.1%	-29.8%
Export	4.0%	6.6%	3.3%	-7.4%	-7.6%
Import	8.0%	7.4%	9.2%	-10.9%	-19.4%
Other items					
Poverty, share of population below poverty line	25%	23%	21%	33%	46%
NIS/US\$, annual average	3.47	3.81	4.14	4.08	4.08
CPI, annual change	7.6%	5.6%	5.5%	2.7%	1.3%
Annual Closure Days	57	15	7	52	210
Population, mid-year (1,000)	2,628	2,731	2,842	2,966	3,096

Note: All data excludes East Jerusalem

Sources: World Bank Staff Estimates, Palestinian Central Bureau of Statistics, UNSCO.

⁴¹ All data excludes East Jerusalem. Sources: World Bank staff estimates, Palestinian Central Bureau of Statistics, UNSCO. Poverty rates for 1996-1998 (year averages) are based on World Bank staff calculations using data from PCBS. For 1999-2001 (year end) poverty rates are based on Bank staff estimates.

3.37 A combination of supply and demand effects underlie the decline of the economy. On the supply side, growth was affected by the rise in operational costs due to internal and external closure. Allocative and technical efficiency was reduced, leading to a decrease in overall productivity.⁴² In addition, capital resources were damaged or destroyed, further diminishing the productive capacity of the economy. The decline in income resulting from this effect, combined with lower remittances from Israel, led to a fall in the overall demand for Palestinian goods, thereby reinforcing the contraction of the economy.

3.38 **Balance of Payments and Remittances.** Balance of payments (BOP) data are patchy in the West Bank and Gaza, as the absence of a national currency limits the use of traditional instruments to measure inflows and outflows of capital. In 1999, the last year for which PCBS produced BOP data, the category “Other Financial Inflows” in the accounts, a residual category,⁴³ amounted to \$958 million, or more than the estimated amount of worker remittances from Israel (\$687 million). As it is not really clear what this category contains, it is difficult to measure how the *intifada* has affected net capital flows. On the one hand, worker remittances and foreign direct investment have certainly declined. On the other, private or public remittances sent to relieve hardship and directly support the families of those killed or injured most likely increased. With suitable caveats, the Bank has estimated that net inflows of capital decreased by \$40 million in 2000 and possibly by another \$100 million in 2001. Summing these capital declines with the loss of worker remittances, and allowing for higher import prices, it is estimated that the capacity of WBG to import decreased by \$168 million in 2000 and by another \$336 million in 2001.

**Table 7: Balance of Payments 1999
(US\$ million)**

Exports of goods & services	727
Imports of goods & services	-3144
Net Factor Income	754
Net Official Transfers	347
Current Account	-1316
Capital transfers	227
Direct Investment	102
Portfolio Investment	-58
Other Financial inflows	958
Error and Omissions	52
Change in reserves assets	35
Capital account	1316

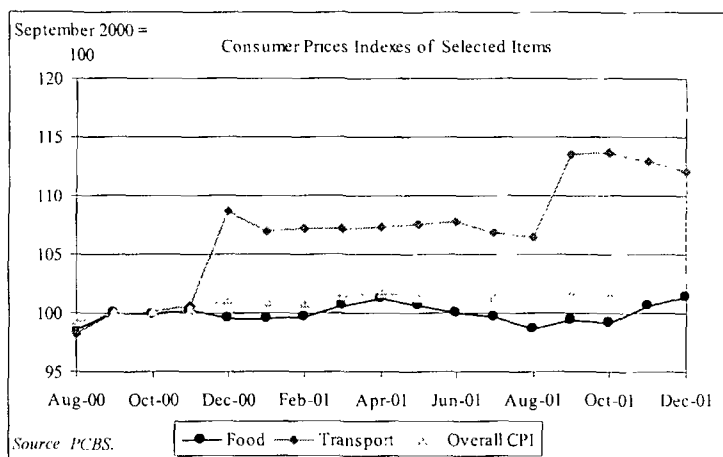
Source: PMA.

⁴² In other words, less goods and services were produced with a given amount of available resources (labor, capital, land).

⁴³ This category groups “all transactions in financial assets and liabilities which are not classified under the categories of direct and portfolio investment”.

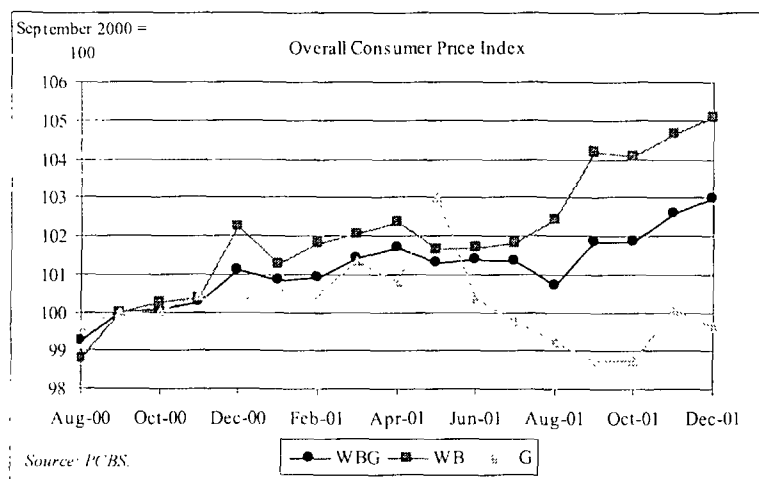
3.39 **Prices.** As a result of the decline of both supply and demand, price levels have been virtually unaffected – in particular, prices of essential goods, notably food items, have been relatively stable since October of 2000. Transport prices are the main exception, rising by 15 percent between September 2000 and December 2001 in consequence of movement restrictions.⁴⁴

Figure 10: Palestinian Consumer Prices, 2000-2001



3.40 This general trend masks significant differences between the West Bank and Gaza, and within the West Bank. In the West Bank there is evidence of sharp local variations in food prices between localities, due to transport problems. In food-producing areas, prices have been severely depressed because goods cannot reach the market, while in non-agricultural areas – especially larger cities – food prices have risen steeply because of the relative scarcity of these same goods.

Figure 11: Consumer Prices in the West Bank and in Gaza, 2000-2001



Overall, the West Bank seems to have been worse affected by these supply factors, leading to some upward pressure on prices. Gaza, by contrast, has been more affected by demand factors – declining income and a reduced consumer capacity to purchase. In combination with tighter restrictions on exports, this has exerted a downward pressure on prices.

3.41 **Private Sector Activity.**

On the eve of the *intifada* there were approximately 56,000 business units in WBG, over

90 percent of them family- or solely-owned small/medium enterprises (SMEs⁴⁵) or micro-businesses. The private sector altogether employed 334,000 people, or 52 percent of the total Palestinian workforce,⁴⁶ and contributed 88 percent of GDP.⁴⁷

⁴⁴ Methodological considerations preclude the comparison of the transport price index from PCBS with the results of the World Bank survey on transport costs.

⁴⁵ With fewer than ten employees in total.

⁴⁶ PCBS and IMF staff estimates for Q3/2000. This number includes the employees of local authorities and public enterprises.

Table 8: Small and Medium-sized Private Sector Units and Employment in WBG, 2000

<i>Sector</i>	<i>Number</i>	<i>Employees (Average)</i>
Primary Sector (agriculture)	193	5.76
Secondary Sector (manufacturing)	11,934	4.51
Tertiary Sector (services)	38,123	1.92
All Sectors	50,250	2.55

Source: IFC SME Sector Study.

3.42 Most businesses in WBG are in the service sectors (retail, hotels, restaurants, business services), although manufacturing and industry (food and beverages, metal fabrication, textiles/garments and furniture) are also important in terms of employment. A combination of political uncertainty and inconsistent public policy has so far inhibited the modernization of the sector. The business culture in WBG is predominantly informal, depending on personal contacts and family relations. Average gross capitalization is only \$10,000, and debt-to-asset ratios are held low due to widespread reluctance to carry formal debt, combined with conservative long-term lending policies in the banking sector. Rather than contracting formal debt, the general practice is to use savings or informal loans to finance business expansion, something that can quickly lead to cash flow problems in a crisis. Traditional links with Israeli businesses have at times inhibited innovation; it tends to be the Israeli partner who interfaces with the international marketplace, and is thereby exposed to international standards and ideas. As a result of these factors, only an estimated 23 percent of private sector earnings came from exports in 1999. This meant that Palestinian businesses felt the full force of the collapse of internal demand.

3.43 Since the outbreak of the *intifada*, employment in the domestic private sector has fallen by some 70,000 jobs, or about 18 percent of its pre-*intifada* workforce. This reflects the grave problems of operating in an isolated environment plagued by weak demand, high transaction costs, supply problems and a lack of any significant programs of emergency assistance to the sector. The private sector's contribution to GDP has fallen from 88 percent to 69 percent of a considerably smaller economy in 2001.⁴⁸

3.44 The major problems faced by the private sector as a result of the crisis were surveyed by PalTrade (for the *Assessment*), and by Center for Private Sector Development (CPSD), which made its results available for this report.

3.45 According to these sources, problems faced by the private sector since September 2000 include:

- *A collapse in revenues resulting in severe liquidity problems.* In CPSD's survey, 94 percent of surveyed firms reported a drop in sales and profits (by an average of 47 percent). These losses were compounded by the increases in transaction and operation

⁴⁷ PCBS and World Bank data. Based on the contribution of private activity in total GDP at factor costs. Private activity is defined as total activity minus public wages.

⁴⁸ According to the World Bank, private sector GDP (at factor costs) was projected to reach US\$3.8 billion (1998 prices) by the end 2001 in the absence of the *intifada*. The projection has now been revised to US\$2.7 billion.

costs, estimated by firms to average 26 percent. Border closure has added significantly to transportation/distribution and storage costs, which rose in the sampled firms by an average of 56 percent; damage to goods in transit also increased by an average of 20 percent (31 percent for agricultural businesses). Firms appeared to be working at about 50 percent of capacity, compared to 85 percent prior to the crisis.

Box 7: A Hotel on the Brink of Bankruptcy

The table below shows the impact on a hotel which was forced to cease operations due to the loss in revenue as a result of the drop in tourism. Although the hotel is not operational, it is still incurring costs such as interest on loans and the salaries of security and maintenance personnel. The hotel is not able to service its debt and overdue interest has accumulated. It has also suffered physical damage from the conflict.

<i>In US\$ 000</i>	<i>Revenues</i>	<i>Net Profit/Loss</i>	<i>Total Liabilities</i>	<i>Current Assets</i>	<i>Total Assets</i>
Sept. 2000	2,366	416	4,363	808	7,543
Sept. 2001	0	(747)	4,308	36	6,250
% Change	-100%	Non-meaningful	-1%	-96%	-17%

Box 8: A Construction Materials Manufacturer and Liquidity Shortage

The table below shows the impact of the *intifada* on a construction materials manufacturer who is currently operating at 65% of production capacity. Raw material costs increased due to higher transportation and import costs as a result of the closures and movement restrictions; these increases in production costs are reflected in the decrease in gross profit margins. The manufacturer has about \$1.3 million in current assets. However, over \$1 million is tied up in accounts receivable, and due to the crisis his suppliers are operating on a cash basis only. As a result, the manufacturer is suffering from severe liquidity shortages.

<i>In US\$ 000</i>	<i>Revenues</i>	<i>Net Profit/(Loss)</i>	<i>Gross Profit Margin</i>	<i>Total Liabilities</i>	<i>Current Assets</i>	<i>Total Assets</i>
June 2000	1,771	24	14.3%	1,761	1,670	3,350
June 2001	1,321	(59)	7%	1,999	1,340	3,445
% Change	-25%	Non-meaningful		14%	-20%	3%

Box 9: Small and Medium Enterprises

Before the Palestinian uprising began in late September, Abu Shaban employed 125 workers building two new schools. Now the projects have stalled, the workers have been laid off, and the payroll has dwindled to a few watchmen at the idled job sites. "Everything's stopped--no materials, no money," said Abu Shaban. *Source: The Washington Post, Sanctions Suffocating Gaza's Fragile Economy, December 6, 2000.*

Nasri Issa Saleh, 52, a veteran trucker, carries plums six days a week from Beit Ummar, just outside the southern city of Hebron, to the main market of Nablus in the north. The road closure has brought economic activity in the region almost to a standstill. As a result, total income from Hebron's plum harvest has dropped from \$2.5 million last year to \$250,000; Saleh says his own income has plunged by 75%.

Source: Newsweek International, Road Rage and the Intifada, July 30, 2001.

- *Credit Issues.* The banking sector has traditionally been risk averse, not only because of the uncertain political situation, but also due to a lack of confidence in the contractual environment. These perceptions were reflected in low loan-to-deposit ratios compared to other countries in the region.⁴⁹ To mitigate high credit risk, local banks lend short-term

⁴⁹ Prior the crisis, the credit to deposit ratio did not exceed 30 percent in WBG, against more than 80 percent in other Middle East and North African countries (World Bank, *World Development Indicators 2000*).

and apply restrictive collateral requirements. Understandably, this approach has been further tightened throughout the past 15 months: the reasons which led private banks to adopt cautious lending policies before the *intifada* are more pertinent today than ever. Although the banks were often criticized for this conservatism prior to the crisis, it proved to be prudent in the *intifada*, and has likely kept intact Palestinian depositor confidence in the banking system.

**Table 9: The Impact of the Crisis on the Financial Sector
(US\$ billion)**

	September 2000	December 2001
Private sector Deposits	3.54	3.21*
Credit facilities to the private sector	1.49	1.18*
PSE capitalization	0.94	0.72

*As of November 2001.

Sources: Palestinian Monetary Authority; Palestine Stock Exchange website.

- *The domestic policy environment.* Firms interviewed for the *Assessment* reported a persistence of burdensome administrative procedures, favored treatment for the well-connected (including through public sector-owned or endorsed monopolies) and a legal system that affords little protection to investors. Pre-*intifada* studies have also detailed the need for a more open, competitive and fairly-regulated business environment. The IFC's Foreign Investment Advisory Service recently released a survey of firms' views on key obstacles to investment,⁵⁰ and found that many of the constraints perceived by investors relate to the policy environment. These views should be balanced by reference to the findings of the World Bank's *Governance and the Business Environment*. This study found that corruption was considered by investors to constitute much less of a problem than in other Arab countries in the region.⁵¹

Table 10: Perceptions of Impediments to Investment

Negative Perceptions/Reasons Not to Invest	Number of Times Cited
Weak legal and regulatory environment	78%
Corruption/PA involvement in the economy	47%
Lack of information on the economy	47%
Lack of infrastructure and facilities	26%
Weak law enforcement and courts system	16%

Source: FIAS Interviews, July 2000—19 firms surveyed who had not invested in WBG.

3.46 The Financial Sector. A particular concern arises from the pressure of PA arrears on private suppliers and thereby on commercial bank loan portfolios. Of the estimated US\$450 million in public sector arrears (Figure 9), between US\$265-290 million appears to be owed to the Palestinian private sector.⁵² Although the quality of bank assets remains officially

⁵⁰ *Enhancing Prospects for Foreign Direct Investment in the West Bank & Gaza, FIAS, August 2001.*

⁵¹ *Governance and the Business Environment in West Bank/Gaza, Working Paper No. 23, May 2001.*

⁵² The extent and composition of PA arrears is currently under review. Current estimates suggest that of the total of US\$450 million in total PA/municipal debt as of the end of 2001, upwards of US\$120 million was owed to the PA pension plans, US\$25 million in social welfare payments was overdue, and over US\$20 million was owed by the

sound (as a result of rescheduling), IFC sample surveys (**Annex 7**) suggest that non-performing loans may by now exceed the capital base of some locally incorporated banks – meaning that they are, in reality, insolvent. Estimates of non-performing loans vary from bank to bank but are estimated by IFC to range between 10-20%.

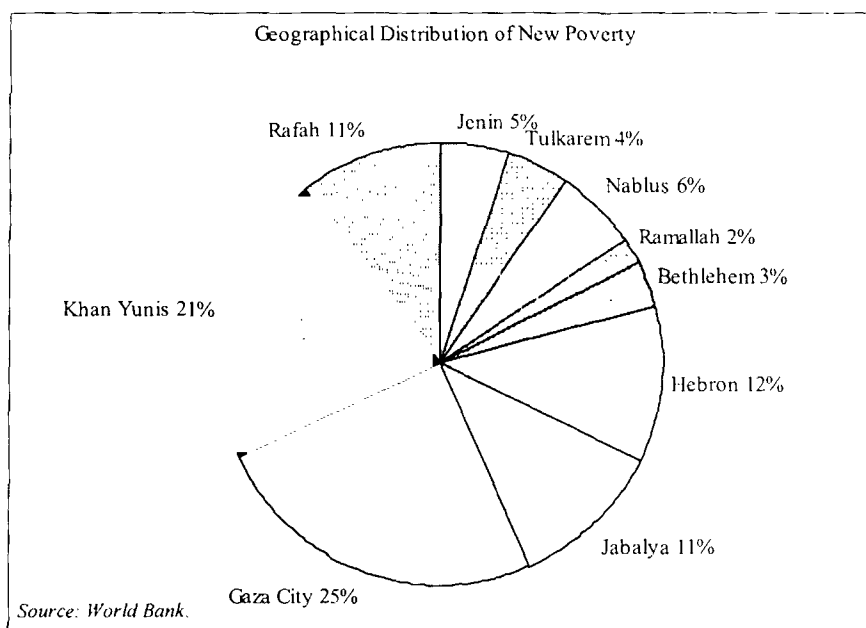
SOCIAL IMPACT

Poverty

3.47 Those worst affected by the crisis have tended to be those who were already poor. There are two reasons for this. The first is that the poor are by definition more vulnerable to economic crisis than those with assets or savings, or with access to networks that do. The second is that the regions where the poor were clustered before the crisis are ones that have suffered badly from closure, be they in the south of the Gaza Strip or in the more remote villages of the West Bank.

3.48 The World Bank estimates that 21 percent of the Palestinian population was poor in September 2000, and that this ratio had risen to 33 percent by January 2001.⁵³ Poverty projections over a longer period of prolonged closures – more than three months – are more difficult to make, as the West Bank and Gaza have never experienced this before. With suitable caveats, then, the Bank estimates that 40 to 50 percent of the population had fallen below the poverty line by the end of 2001.⁵⁴

Figure 12: The New Poor

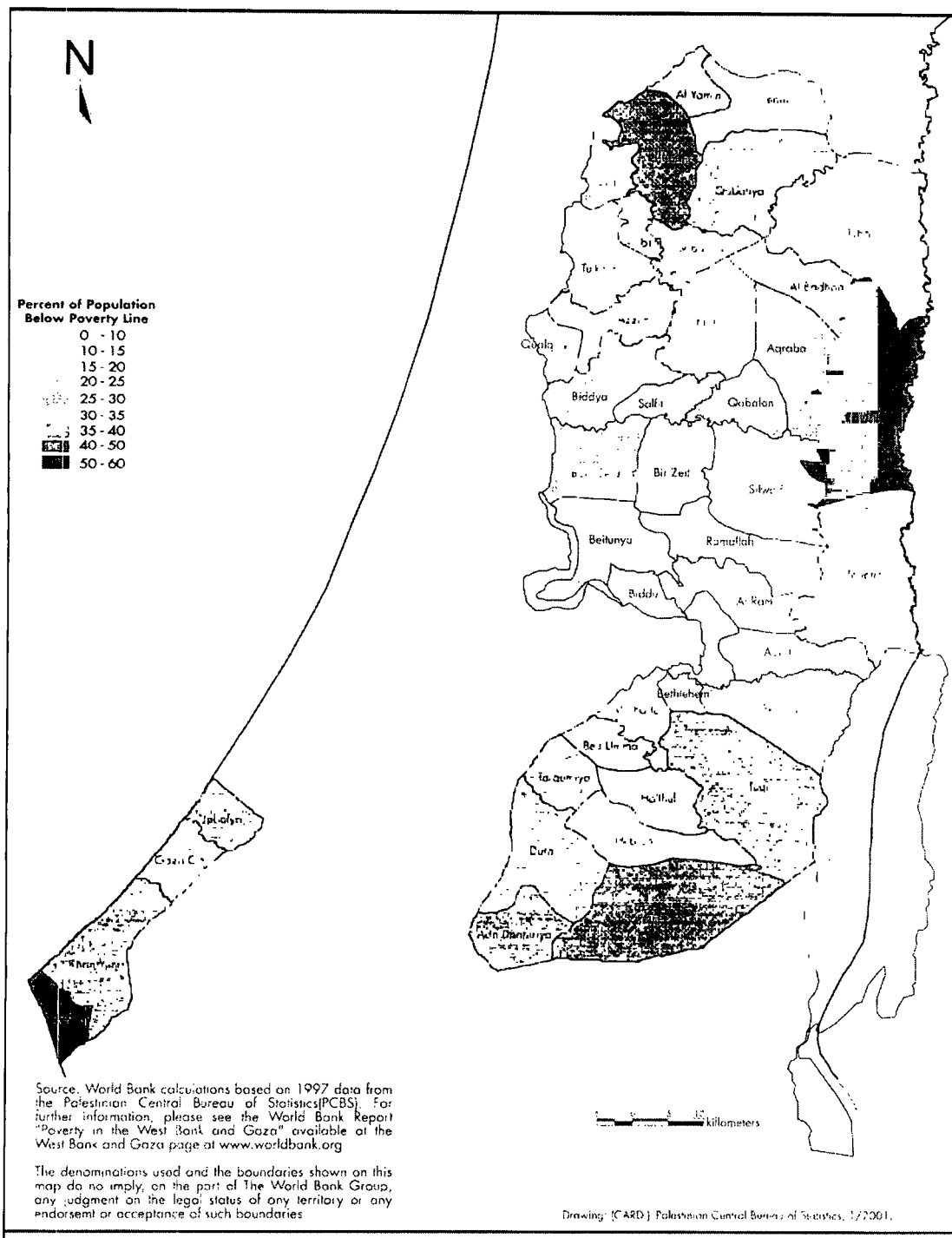


PA and the municipalities to Israeli suppliers. These figures still need to be confirmed/adjusted by the Ministry of Finance.

⁵³ When PCBS last measured poverty based on household consumption (in 1998), 23 percent of the population was considered poor. See *Poverty in the West Bank and Gaza* (2001), World Bank, for an account of Palestinian poverty since 1996 and a description of the different methods used to forecast poverty.

⁵⁴ One can also measure poverty by income levels. According to this measure, PCBS estimated that 65 percent of the Palestinian population in July 2001 were living under a poverty line of NIS 1,622 for a typical household consisting of two adults and four children. A survey conducted in November 2001 on a sample of 1,598 respondents estimated that 42.3 percent of the population in West Bank and Gaza (excluding East Jerusalem) was living under a poverty line of NIS 1,600 per month per household (*Palestinian Public Perceptions on Their Living Conditions*, Graduate Institute of Development Studies, University of Geneva, Report III, December 2001). These two estimates

Map of Poverty (as of 1997)



are based on the reported monthly income of the households. Unfortunately there are no pre-crisis estimates of poverty using the same definition. A more robust method of measurement of poverty is to use consumption data. Consumption measures capture the impact of coping strategies – such as the use of savings, sales of assets, borrowing and welfare receipts – and these coping strategies need to be considered alongside income to assess well-being. It is also axiomatic that households are more reluctant to report incomes than consumption patterns. See for instance Ravallion (1992), *Poverty Comparisons: A Guide to Concepts and Methods*, The World Bank.

3.49 Whatever the increase in poverty at the national level since September 2000, it has not been equally spread across all localities. Particularly affected were the remote villages of the West Bank and the southern part of Gaza, all of which lost contact with the labor and goods markets of Israel and the larger Palestinian towns. Based on a model relating employment status to poverty, the World Bank estimates that 2/3 of the persons who have become poor since October 2000 – the “new poor” – are to be found in the Gaza Strip, with almost half in Gaza City and Khan Younis. In the West Bank the largest concentration of new poor is in the Hebron area. At the other extreme are the Ramallah and Bethlehem areas, with only five per cent of the new poor. The lack of consistent data precludes further disaggregating this map of new poverty, but it is likely that the distribution of poverty across localities has not changed much since September 2000, with the poorest areas having suffered the most from the crisis. A detailed poverty map was recently produced with data from 1997, and it would be advisable to use this information to determine emergency intervention priorities (e.g. the distribution of employment programs).

Household Coping Strategies

3.50 Two quantitative surveys conducted in Spring 2001 by PCBS and the Bir Zeit University provide information on how households have coped with prolonged closure and reduced incomes. The results are borne out by comparable conclusions from qualitative surveys of two West Bank villages and two WBG towns conducted by the Norwegian research institution Fafo.⁵⁵ Although they permit households to maintain a minimum level of expenditure, most strategies adopted are unsustainable in the long run, as they either reach intrinsic limits or risk an irreversible reduction of the productive capacity of the household.

Table 11: Strategies Adopted to Cope with Closure and Reduced Income

<i>Coping strategies</i>	<i>Bir Zeit U (Feb 2001) By percentage</i>	<i>PCBS (April 2001) By percentage</i>
Reduced expenditure	84	81
Used personal savings	55.2	41.6
Delayed bill payments	n.a	55.4
Borrowed money	42.9	35.9
Sold jewelry/personal effects	22.3	18.2
Turned to farming/livestock	16.9	12.1
Sold/ mortgaged property or lands	4.1	1.5
Remittances from abroad	n.a	2.7
Sent family member abroad	n.a	2.3
Changed residence	n.a	0.6

3.51 More than 80 percent of respondents claimed to have reduced their expenditures. For lack of more detailed data, it can be assumed that expenditure reductions were accounted for mainly by reducing the purchase of non-essential and “luxury” items. However, the surveys also reported a significant decrease in consumption. Most poor households were facing difficulty in purchasing basic food products, principally animal protein and fruit. Animal protein consumption declined from twice per week to once or twice per month (on average). Those

⁵⁵ *Paying a Price: Coping with Closure in Two Palestinian Villages; Paying a Price: Coping with Closure in Gaza City; Paying a Price: Coping with Closure in Jericho*. Fafo, Norway, 2001.

interviewed indicated that most families were substituting for animal protein with lentils, chickpeas, vegetables, eggs and *za'tar* (thyme) - traditional locally produced foods that are less expensive. Milk powder was often diluted for babies and children.⁵⁶ Approximately half the respondents also said they had used their personal savings to purchase food and other basic goods. These findings are consistent with the Bank's study on poverty, which showed that Palestinian households initially responded to previous extended closures by spending their savings (so-called "consumption smoothing"). With the period 1998-2000 one of few border closures, the average household had accumulated savings equal to about 2.75 months worth of consumption expenditures.⁵⁷ On the assumption that the average income has been reduced by almost a half, and average consumption by one third, this level of savings would permit households to maintain a reasonable level of consumption for 17 months in all, i.e. until the spring of 2002. However, savings are obviously not equally distributed across households, and many of the poorest households exhausted whatever they had many months ago.

3.52 The PCBS surveys reveal that more than half the population delayed payments and more than one-third incurred debt. In the West Bank the majority of localities visited mentioned their inability to pay basic household utility bills (water, electricity and telephone). Interviewees indicated that, on average, households were holding three outstanding utility bills. PCBS found that although 36 percent of respondents reported borrowing money, only 5 percent did so from banks or financial institutions. Most borrowing was done informally, from family members and local shops and retailers, as was the norm before the *intifada*. This approach has obvious limits in the absence of external support, as persistent economic pressure reduces people's ability to assist one other. Only 3 percent of respondents said they had received remittances from abroad (though it is not clear from the survey whether Jordan is considered "abroad" in the conventional sense by all respondents, since families are often split across the two banks of the Jordan river).

Box 10: Closure in Two Villages --Rantis and Beit Furik

During the first half of 2001, the Norwegian Research Institute FAFO undertook a study in two villages in the West Bank, Rantis and Beit Furik, with the aim of describing how Palestinians live when they have been partially closed off from communication with the outside world. The results of this work in many ways mirror the *Assessment's* macro-level conclusions.

The study describes in great detail the obstacles the villagers face as well as the ways and means that they employ in their daily life to make ends meet. Its main findings can be summarized as follows:

1. For a household it is crucial to have members that can either still work in Israel or who still receive steady wages. Those who do not must depend on their relatives. Those who are without sources of income themselves and who have no such network are the worst off.
2. Direct transfers to households from relatives abroad appear to have minimal or no importance. Organized external aid to individual households is handed out occasionally. Such aid is helpful, but does not make a crucial contribution to the survival of households.
3. Villagers tend to perceive aid programs negatively: several externally financed development projects have been postponed, thereby depriving the communities of an improved quality of life in the medium term, and construction work in the short term.

⁵⁶ Another PCBS survey of July 2001 asked respondents about reductions in nutritional consumption, and found that 35 percent reported a reduction in the quantity of food, 55 percent in the quality of food; 65 percent in the quantity of meat; 65 percent in fruit and 43 percent in milk and milk products. Perhaps surprisingly, the reduction in the quantity of food and in milk and milk products was significantly higher in the West Bank than in Gaza. This may be accounted for by the relatively higher pre-*intifada* consumption patterns in the West Bank.

⁵⁷ UNSCO estimate.

4. Basic services such as electricity and water have been maintained, but water supply was never adequate.
5. Schools and clinics have faced very difficult working conditions, but are still able to function.
6. There are two key reasons for why the closure has not had even more drastic consequences. The first is that the Palestinian Authority still pays salaries to its staff. Salaries are generally paid whether or not staff are able to show up at work. Second, even though the closure is strict, it is not total. Workers are intermittently able to carry on working in Israel, and to receive wages that are much higher than they could obtain for equivalent work in the West Bank.
7. Another important factor is the widespread willingness of shopkeepers and service-providers to extend credit. Nevertheless, there are clear signs that this system is in danger of breaking down, with those who are providing credit unable to sustain it indefinitely.

If the closure tightens or persists at current levels for a protracted period, and especially if the Palestinian Authority is unable to pay wages, a far greater economic crisis would descend on these two villages.

Source: Fafo, 2001.

3.53 Regarding the sale of belongings, the Bir Zeit and PCBS polls came up with comparable findings, and showed a much higher incidence in Gaza than in the West Bank. Sales allow households to increase liquidity, but forced sales in a depressed climate yield low prices and reduce capital, thereby dampening the capacity to rebound once the overall situation improves.

3.54 Prior to the *intifada*, agricultural work had become largely a source of supplementary income, and often left to those not otherwise wage-employed, such as women and the elderly. The current reversion to agriculture has led to a doubling of those spending time in agricultural work, with the phenomenon more prevalent in the West Bank than in Gaza.⁵⁸ One negative effect of this, should the pattern persist, is a substitution of high value-added products destined for export by low value-added products for local consumption.

3.55 Finally, around 2 percent of respondents said that family members had gone abroad for extended periods. Anecdotal information suggests that many of those leaving are highly-skilled and internationally mobile, exactly those that Palestinian society can least afford to lose.

Box 11: Closure in Gaza and Jericho

Fafo also carried out two studies in the cities of Jericho and Gaza City in Spring 2001, to understand how closure affects the daily life of urban households.

These two case studies also show how closure increases transaction costs, and hinders the exchange of goods with other areas. Export-oriented activities, such as agriculture and tourism in Jericho, have suffered particularly badly from closure. Access to the Israeli labor market (in Israel and the settlements) has become more difficult from Jericho, and almost impossible from Gaza City. In turn, reduced incomes have led to a fall in the demand for locally produced goods.

The two local economies did not collapse, since their internal markets remained. This constitutes the main difference from the situation in the villages, where the critical mass of economic agents is not large enough to maintain a minimum level of economic activity in a quasi-autarkic situation. Closure created some new income generation opportunities in Gaza City through import substitution, with the local market “protected” against certain consumer products – a phenomenon not observed in the villages.

⁵⁸ This reversion to agriculture is not, however, reflected clearly in the macro statistics: In the West Bank, the share of workers employed in agriculture, fishing and forestry has remained constant throughout the crisis at around 13 percent, while it decreased in Gaza from 17 percent in Q2/2000 to 12 percent in Q2/2001 and remained at that level until end-2001. One explanation may lie in the fact that surveyed workers do not consider agricultural work as their main professional activity.

The two studies again underline the crucial role played by salaries paid to Palestinian Authority employees, which continued to inject liquidity into the local economies.

The fact that most of the coping strategies adopted by households (selling assets, spending savings, eliminating non-essential consumption, extending credits) are not sustainable in the long run further reinforces the importance of maintaining public service activities, which are mostly concentrated in the cities.

Source: Fafo, 2001.

Box 12: Stories of Personal Hardship

Samir -- little left

Samir is 42 and lives in Deir El Balah Camp; he has seven children, the eldest a girl of 12.

Samir always worked in Israel as a construction worker. He earned NIS 3,500 per month. He started to build a 3-room house for his family. Before he could finish it, he lost his job, in August 2000, and has not been able to find work again since. Even though he was given a permit to work in Israel in May 2001, no jobs have been available.

He has tried to find support from all possible sources. Since November 2001 he has received

A loan of US\$700 from UNRWA

One-time cash assistance of US\$300 from UNRWA

Three food packages from UNRWA (flour, sugar, lentils, milk, oil--the flour lasts 17 days)

One-time cash assistance of NIS 600 from the Workers Union

One food package from the Salah Committee

His house still has no doors. Samir has so many debts that he feels uncomfortable to leave his house: He owes NIS 4,000 for electricity bills, NIS 1,500 for water, NIS 300 for gas and NIS 2,000 to friends. He came to the ministry to ask for a bag of flour because he had nothing left to eat in his house.

Interview with Samir conducted on January 20, 2002 in a local Office of the Ministry of Social Affairs in Gaza.

Manal – a single bag of flour

Manal is 27 years old. She comes from Zaitoun, an area of Gaza City. Her husband is 32 and they have six children.

The family lives in two rooms belonging to the *Waaf*. Before the *intifada* her husband worked as a mechanic in Israel and earned NIS 2,400 per month. This was enough and they had managed to buy some gold as savings. Since October 2000 he has not been able to go to his work because he has not been able to receive a permit.

The family has tried to find help. They have received

One month's work for her husband for NIS 800 under the PA's job creation program

Cash assistance from the Workers Union on two occasions – NIS 600 and NIS 500

Food packages of flour, milk, rice and sugar from a local committee

One-time cash assistance of NIS 100 from their Zakkat committee

In late 2000 Manal sold the gold they had saved. Now they survive with the help of her family and neighbors. Her brother gives her NIS 500 per month and her mother another NIS 50, but this is not enough. Manal said they could manage if they could get another NIS 400. She came to the ministry to ask for in-kind assistance. She has not received anything from the ministry to date, but was promised a bag of flour for the following week.

Interview with Manal conducted on January 20, 2002 in a local Office of the Ministry of Social Affairs in Gaza.

Amal, a special hardship case

Amal is a widow with 12 children, the eldest of whom is 19 years old. Three years ago her husband who was a worker in Gaza, fell sick. Since then the family has been classified as a Special Hardship Case of the Ministry of Social Affairs. A year ago, Amal's husband died. They had already accumulated debts of about NIS 10,000 by that time.

Amal gets the maximum support possible from the Ministry: cash assistance of NIS 572 per month, which is based on the number of people in the family; food aid (in 2000, four times: in March (flour and sugar), June (rice and

sugar), September (rice and olive oil) and November (flour and olive oil). The ministry also pays her family's health insurance and school fees (NIS 40 per child per year).

Last year cash assistance was not paid for about six months, she thinks, though she recently received one payment. Amal then bought on credit from the neighborhood mini-market. Her cousin and her brother in law also help out sometimes by sending food for the family. Amal's biggest hope is her 17 year old son. He will finish school next year and will then, she hopes, be able to work and look after the family.

The interview with Amal was conducted on the January 22, 2002 in her house in Toffah, Gaza.

Mahmoud – sickness and the poverty trap

Mahmoud is 40 years married with 5 children. Until 1999 he worked in Israel. He and one of his brothers started to built a house. In 1999 he was diagnosed with cancer of the kidney. One of his kidneys was removed, but he never totally recovered and is an invalid.

Since 1999 the family has been classified as a Special Hardship Case, receiving NIS 386 per month in cash assistance, food support about four times per year and health insurance and school fees for the family. He cannot manage with this, so his brother, who works for the Police, gives him money each month. Now, though, the Ministry does not always pay his benefits on time; last year there was a gap of for four months during which he received nothing. The smaller children need milk and clothes, and the house is still not finished. Mahmoud's eldest son is 12 years old and has several years of school before he can earn. Mahmoud is too sick to participate in any rehabilitation program, and he knows his family will need help from the Ministry for years to come.

The interview with Mahmoud was conducted on January 20, 2002 in his house in the South of Gaza City

Source: World Bank.



4. THE INSTITUTIONAL RESPONSE

OVERVIEW

4.1 Confrontation, restrictions on movement and the compression of operating cost budgets impaired the PA's ability to interact with donors and civil society and to formulate a unified response to the crisis. In consequence, the management of the crisis has been fragmented between different ministries and agencies. Despite this lack of overall guidance, a number of PA organizations deserve particular credit for their performance: the Ministry of Finance for establishing and holding to a hard budget ceiling; the ministries of Health and Education for concerted efforts at a sectoral level, in close coordination with donors and NGOs; PECDAR, as an implementer of job creation infrastructure projects, and the municipalities, which have adjusted to constrained budgets and have for the most part continued to deliver services. When the scale of the challenge is considered, PA performance has been impressive. A minimum level of service delivery has been sustained under very adverse conditions, though this is becoming increasingly difficult as the fiscal situation deteriorates.

4.2 Several larger non-governmental organizations have received significant additional funding during the *intifada*, enabling them to help meet the increasing social needs of the population. However, many small NGOs faced budgetary problems as their traditional domestic sources of funding sharply decreased. More recently, many NGOs affiliated with *Hamas*⁵⁹ have been closed, creating significant potential gaps in emergency and non-emergency services alike.

4.3 The United Nations Relief and Works Agency for Palestinian Refugees in the Near East (UNRWA), always an important player and charged with providing social services to the refugee population (constituting about half of the total population of WBG) has played an important role in supporting the social fabric over the past year.

4.4 Donors have encountered major implementation problems; closure has interrupted the movement of donor personnel, increased costs and delayed the delivery of project materials, while conflict has led to the destruction or damage of facilities and/or has impaired their operation; it has also put many international experts off working in WBG. Nevertheless, donors have responded to the challenge and have provided a vital safety net for the Palestinian people during the *intifada*. Most donors have adjusted their programs to cater to the emergency, in particular by providing budget support to the PA and by financing job creation and welfare programs. The efforts of Arab League states, mostly channeled through the Islamic Development Bank, have been particularly notable and have accounted for almost half of all donor disbursements in 2001.

⁵⁹ *Haraket al-muqawama al-islamiya* (Islamic resistance movement).

THE RESPONSE OF THE PALESTINIAN AUTHORITY

Budget Management and Emergency Coordination⁶⁰

4.5 Faced with a fall in revenue from closure and then by Israel's decision to stop the transfer of clearance revenues in December 2000, the Palestinian Authority responded by cutting expenditures, borrowing from the domestic banks and appealing to donors for *ad hoc* budget support. Access to commercial bank credit was soon exhausted, and the PA has been forced to rely on donor contributions and on forced credit from suppliers.

4.6 In response to the fiscal crisis, the PA cut spending from a monthly average of US\$107 million in the third quarter of 2000 (and a high of US\$110 million in December 2000) to a monthly average of US\$90 million under the April – September 2001 *Six-Month Spending Plan* formulated by MOF in April 2001 with the assistance of IMF staff (and *de facto* renewed since October 2001). This Plan assumed that Israel would resume the transfer of revenue clearances to the PA, and committed the PA to a significant slow-down in new public sector recruitment, while aiming to secure the employment of those already on the payroll. This was a defensible decision, since these salaries helped to sustain a minimum level of demand in WBG. After salaries, priority was given to emergency expenditures, programmed at a monthly average of US\$17 million in the first three months of the Plan. This left only US\$17 million per month for non-emergency operational costs and investment expenditures, as compared to US\$54 million per month in the third quarter of 2000.

4.7 Israel, however, continued to withhold revenues due the PA. Even with domestic revenue performance better than projected in the *Spending Plan* and with donor support slightly higher than anticipated, the PA's monthly cash shortfall averaged US\$20 million from April to December 2001. As noted in **Chapter 3**, the shortfall was mediated by forced credit from suppliers (unpaid bills) and by *ad hoc* reductions of non-wage recurrent expenditures.⁶¹

4.8 What has so far been lacking, though, is a shared governmental vision of how to manage the crisis. A number of emergency response plans have been drawn up, notably by the President's Office, the Ministry of Planning and International Cooperation (MOPIC), the Ministry of Finance and PECDAR (see **Annex 4**), but these have tended to be written in isolation and have not been universally adopted. Nor has any apex-level forum been established to manage the crisis. Inter-ministerial coordination was often problematic before the *intifada*, and the crisis has not dispelled the problem. Thus, for example, there is no clearing mechanism in which MOF and the spending ministries review financial demands and jointly agree emergency priorities. Although employment generation programs have formed an important part of the PA's response to the crisis, there is little programmatic coordination between the various bodies involved (such as PECDAR, the Ministry of Public Works, the municipalities, the Ministry of

⁶⁰ See also **Annex 2**.

⁶¹ For example, contributions to the PA's pension schemes and monthly payments to social hardship cases on the Ministry of Social Affairs' register--para. 4.38.

Finance).⁶² This has made it more difficult to exchange ideas and share experiences, as well as to present coherent funding proposals to donors.⁶³ These issues are further explored in **Chapter 5**.

4.9 At a technical level, moreover, the essential information systems needed for coherent planning have been lacking. For example, development of fully-articulated public expenditure accounts would enable MOF to monitor and manage the detailed budget allocation to line ministries. Reviving the MOPIC data base on donor activity, an essential underpinning of the aid management effort, would permit a proper awareness of where funds are flowing and which key initiatives remain under-funded.⁶⁴ It is important to note that the PA/donor coordination mechanisms established in 1993 also lost momentum over the first year of the *intifada*. In a situation in which the degree of dependence on donor financing is so great and in which economic planning has traditionally been carried out by the PA and the donors together, this left line ministries and agencies without the support they needed to integrate their efforts effectively.

Health Service Delivery

4.10 Demands on the health services rose significantly during the *intifada* on account of injuries and disabilities,⁶⁵ while needs in other areas have not declined. At the same time, resources have contracted.⁶⁶ Providers have sometimes been obliged to work under fire, staff have found it difficult to reach health facilities, and the delivery of supplies has become erratic. The Palestinian Red Crescent Society, working at the forefront of casualty care, reported that 91 of its staff had been injured and 57 of its 75 ambulances damaged in the fighting by the end of June 2001.⁶⁷ The emergency preoccupied all service providers, and most plans to build on the achievements in the sector since 1994 were shelved in the struggle to cope with daily basic health needs.

4.11 **The Sector.** Closures in the West Bank and Gaza have imposed severe restrictions on access to health facilities for both patients and medical personnel. According to PCBS in July

⁶² The Ministry of Finance has for the past six months forcibly deducted two days wages from PA employees in order to transfer some funds from the employed to the unemployed. With US\$2.5 million per month thus collected, cash payments are made to some 23,000 workers each month on a rotating basis (some 140,000 families have thus benefited from one-time cash payments of c. \$100).

⁶³ Seminars held in November 2001 in Gaza and the West Bank between PA agencies and donors revealed a wide difference in the labor content in job creation programs, for example, as well as in unit costs.

⁶⁴ The donor data for 2000 is incomplete and for that reason the *Assessment* has used 1999 as its comparator year for the *intifada* period.

⁶⁵ UNRWA has reported a 20 percent increase in patient numbers in the period.

⁶⁶ MOH spending prior to the *intifada* accounted for about half of total health spending in WBG, over two thirds of hospital bed capacity at the secondary care level, and a significant share of primary care services. MOH also provided financial support through its Health Insurance Program to patients requiring overseas treatment (Egypt, Jordan, and Israel), and increasingly, for health services contracted with NGO and for-profit medical providers in WBG. UNRWA accounted for about one tenth of total health care spending, with a focus on primary care services for the refugee population. The NGO sector accounted for about one fifth of health spending as well as about a fifth of the total hospital bed capacity in WBG. A small for-profit sector, established after 1994, has been providing high-end technology and specialized medical services (e.g. diagnostic imaging, catheterization labs).

⁶⁷ The data in paras. 4.10–4.14, unless otherwise referenced, are from *Vulnerability and the International Health Response in the West Bank and Gaza Strip – An Analysis of Health and the Health Sector, November 2001*, WHO (Draft). WHO kindly consented to the use of this report in compiling the *Assessment*.

2001, 23 percent of households report an inability to reach points of service in a timely manner.⁶⁸ Access problems vary sharply by region, creating what WHO has called acute “pockets of vulnerability” for roughly 40,000 people.⁶⁹

Box 13: Medical Access

Litfiyeh Ibrahim 'Abdallah Jaludi, 41, a married mother of six from the Pequ'a village in the Jenin region, undergoes dialysis treatment for her kidney ailment three times a week at Nablus' Altuni Hospital. Instead of the relatively short route she took prior to the eruption of the *intifada*, her current agonizing, twisting journey along back roads lasts between three to four hours. “The great trouble and difficulty in getting to the hospital is too much for me,” she told B'Tselem [the Israeli Information Center for Human Rights in the Occupied Territories.] A-Saad's and [another patient's] stories are two of the eight cases examined in the new B'Tselem report. In two of the other six cases, patients whose paths to hospitals were impeded died.

Source: Ha'aretz, You can't show medical papers to concrete blocks and deep trenches, June 24, 2001.

4.12 Public health services, such as water/sewage testing, water chlorination and vector control have been interrupted, and there is a growing risk of the spread of infectious disease. Vaccination coverage remains comparatively very high thanks to the combined efforts of MOH, UNRWA, WHO and UNICEF (at 91 percent, down from pre-*intifada* levels of 98 percent). Anecdotal evidence indicates that households are increasingly unable to pay for services and medicines, to the distress of the chronically ill. While some households have been able to buy medicines privately, general impoverishment means an increasing risk of segments of the population falling through the meager public social safety net.

4.13 Mental health effects are difficult to quantify, but attendance at mental health clinics appears to have risen, and the Community Mental Health Department of the Ministry of Health reported a 105 percent increase in new cases registered at mental health clinics, the majority children under the age of 18. Demand for counseling services rose by 72 percent in the West Bank through April 2001. In a household survey concluded in July 2001, PCBS reports a rise in psychological conditions among a majority of children.

Box 14: Children and Trauma

Therapists from the Gaza Community Mental Health Program are counseling increasing numbers of children suffering from post-traumatic stress disorders. Symptoms include thumb-sucking, crying, clinging to parents, nightmares, bed-wetting, poor appetite, poor sleeping patterns, short attention spans, aggression towards siblings or parents, and fear of dying. Several NGOs have organized workshops and set up hotlines to help Palestinians cope with the current situation, including the shelling of residential areas. The latter has resulted in the displacement of at least 4,000 individuals. Many left their homes to live with relatives, some live in makeshift camps.

Sources: The Health, Development, Information and Policy Institute (HDIP), Health under siege II, May 2001.

4.14 **Services.** As the availability of PA funds has diminished, both public and private/NGO providers have been forced to curtail services. This has included the suspension of many long-term development projects (infrastructure, capacity building) and training programs. Resources have been further squeezed by facilities either reducing or waiving patient fees, in part out of

⁶⁸ Despite high coverage, the efficacy of vaccination under present circumstances cannot be evaluated until later, and there is reason for concern given transport delays and the exposure of some vaccines to heat.

⁶⁹ High-risk areas include Shoka, Mawasy, Mograga, Joher Al Deek, Rashayadeh and Ramadeen. A significant portion of the most vulnerable are Bedouin.

responsiveness to increasing hardship among the population, and partly as a result of popular expectations of free treatment under crisis conditions. Across the sector, the struggle to meet monthly salaries and basic running costs has displaced most developmental objectives. The capacity to keep afloat has been strained, and providers are relying to a significant extent on volunteers, employees working unpaid overtime, creditors not actively seeking debt payments, and support from donors. Six health NGOs surveyed for the *Assessment*⁷⁰ that either receive fees from MOH or charge their patients have all taken financial losses -- due to MOH's budget squeeze, patients' inability to pay and a drop in private donations. The Palestinian Red Crescent Society, for instance, was able to sustain its national ambulance service only because of a commitment by the International Committee of the Red Cross to finance running costs to the end of 2001. The private medical sector, especially given its concentration in tertiary care, has been less able to adopt flexible strategies and has had to cut salaries by up to 40 percent, delay payments by as much as two months, and release staff.

4.15 At an operational planning level, MOH has taken impressive steps to lead the response to the health crisis. In early 2001 the Ministry adopted an explicit "decentralization" strategy in which additional authority was given to local health officials, who were also charged with strengthening community participation in healthcare and improving communications between providers in their local areas. As areas were blocked or became disconnected from supply routes, MOH worked closely with UNRWA and NGOs to build mobile health teams and to increase the provision of home care. They also created joint technical teams and pooled facilities, coordinated the distribution of supplies to those in greatest need, and even shared personnel.

4.16 **Resources.** The table below summarizes MOH's planned and actual non-salary recurrent expenditures for 2000 and the first half of 2001. The effects of the *intifada* were already evident in late 2000, with the non-salary recurrent receipts experiencing an immediate 26 percent shortfall compared with originally planned allocations. In 2001 the situation worsened, with actual disbursements from the treasury accounting for only 9 percent of needs by mid-year, although 61 percent of the budget had been "spent" (US\$29.6 million).⁷¹ Due to the *intifada* the demand for health services has risen, and thus the decline in resources is even more acutely felt.

⁷⁰ Hossam Sharkarwi, study commissioned for the *Assessment*.

⁷¹ These two figures are not directly comparable, though, since the US\$29.6 million reported are for the period January-October 2001.

Table 12: Sources of Funding for MOH, Non-Salary Expenditures, 2000 & January-June 2001

	Jan-Dec. 2000				Jan-June 2001			
	Spent US\$ 000	Provided US\$ 000	% of Budget Received	Deficit US\$ 000	Planned for FY2001 US\$ 000	Provided by June 2001 US\$ 000	% of Budget Received	Deficit US\$ 000
Total Non-Salary Recurrent Budget	46,500	34,508	74%	-11,992	49,800	9,483	19%	-40,317
➤ From MOF		34,055	73%			4,527	9%	
➤ From donors		453	1%			4,956	10%	

Source: Finance Department, Ministry of Health, August 2001.

Table 13: Donor Emergency Disbursements to the Health Sector, 2000 - 2001 (US\$ 000's)

Emergency Assistance Categories ^{1/}	Total	
	US\$ (000's)	%
<i>Recurrent Contribution</i>		
- Drugs and Medical Disposables	13,738	24%
- Operations and Maintenance Support to MOH/ ²	4,150	7%
- Patient Treatment (Unspecified)	In Kind/ ³	
- Psychosocial Treatment	896	2%
- Post-injury Rehabilitation Treatment	1,336	2%
- Cash	30	0.1%
Sub-total Recurrent Budget and Technical Assistance	20,150	36%
<i>Capital Contribution</i>		
- Vehicles/Ambulances	1,029	2%
- Construction/Extension	21,122	38%
- Medical Equipment	4,006	7%
Sub-total for Capital Investment	25,128	44%
<i>Unidentified Category</i>	11,294	20%
Total	56,572	100%

Sources: MOH, 7th UN Inter-Agency Meeting, 27-28 June 2001, Gaza; MOH Website: www.moh.gov.ps.

Notes: 1) ongoing non-emergency projects are not included; 2) this figure reflects the actual disbursed amounts from IDB against the US\$10 million committed by the Bank at that point; the figure is thus inconsistent with the equivalent figure in Table 14; 3) IDB is providing free of cost travel and treatment in Saudi Arabian for the injured, the number of which are unknown, and therefore indicated as "in kind".

4.17 These shortages in operating costs have had a number of unintended impacts. Drugs have been provided largely via donor donation during the *intifada*⁷² -- and together with the Ministry's strategy of purchasing drugs on credit from local suppliers, this has had the effect of reducing purchases from a local pharmaceutical industry already suffering a loss of private demand. Drug

⁷² Preliminary data on medical procurements in 2001 show that donors provided almost 62 percent of the total value of medicines acquired since the beginning of the *intifada*.

manufacturers report a 40 percent decline in sales,⁷³ endangering the viability of a number of enterprises.⁷⁴ Despite donations and credit purchases, many important drugs – e.g. for diabetes and hypertension – have become very scarce.⁷⁵

4.18 Due to the sheer size of MOH operations, emergency contributions from donors have had a limited impact on alleviating the MOH deficits. Multiple small donations, many of them in kind, may have inadvertently made it harder for MOH to provide effective services -- by complicating administration and impairing efficiency, through an inability to make bulk tenders and contracts, and due to the unpredictability of supply delivery schedules. With donor support directed to short-term emergency care, other critical health care needs (preventive care, the treatment of chronic diseases) have received little support. A severe cutback on facility and equipment maintenance is compromising health care quality and will in time have serious consequences for health outcomes, while essentials like fuel for the ambulances and contracts with private suppliers/NGOs are significantly under-funded. Thus far, only the Islamic Development Bank has provided substantial support for the MOH recurrent budget (US\$15 million), with this contribution amounting to a third of total non-salary requirements. Further compounding the problem, contributions from the Palestinian health insurance scheme have fallen significantly.⁷⁶

4.19 Meeting the needs under such tight budget strictures has led the Ministry to contract debt to many suppliers, including the non-MOH facilities which continue to provide treatment for *intifada*-related injuries. While the magnitude of debt is difficult to establish, both MOH and the contractors will be hurt badly unless these debts can be settled soon – MOH by the inability of contractors to keep on providing services, and contractors by the eventual collapse of their operations. Under these circumstances, and in view of increasing evidence of shortages of fuel, medicines and spares, the decision to raise the MOH salary component in the 2001 budget (from actual expenditures of US\$46 million in 2000 to an allocation of US\$53.5 million for 2001) should not be repeated in the context of the 2002 budget.

4.20 It is worth noting that MOH was the first among PA ministries to install (with DFID assistance) a financial accounting system. This provides a standard chart of accounts, including the general ledger, accounts receivable and payable, and makes it possible to maintain good recurrent budget coordination with MOF.

⁷³ World Bank health staff interviews.

⁷⁴ MOH estimates that their purchases previously accounted for as much as 40 percent of local drug production

⁷⁵ MOH reports that 130 medications are currently out of stock.

⁷⁶ The revenues from health insurance premia declined by over 40 percent in the first six months of 2001 compared to the first six months of 2000, as few households were able to pay premia due to rising unemployment and earnings losses. Since 2000, MOH has been permitted by MOF to retain fees and co-payments collected at the point of service.

Education Service Delivery

4.21 The quality of education has suffered significantly since September 2000. Teachers, administrators, and students have struggled with movement restrictions, and the focus required for students to learn has been impossible to maintain. The Ministry of Education (MOE) is struggling to keep the system running and to reduce losses in instruction time. And meanwhile, the Ministry of Education must continue to expand the educational system to accommodate a rapidly-increasing population.

Schools

4.22 **The Sector.** In the 18 months prior to the *intifada*, MOE worked to transform itself into a professional and modern organization. In 1994 the PA inherited an educational system from the Israeli Civil Administration four days before the school year was due to open. The new MOE thus began by managing crisis, and high fertility rates in West Bank and Gaza⁷⁷ forced the ministry to focus initially on managing the large annual increases in enrollments.

4.23 However, in close consultation with the donor community, MOE recently began a priority-setting, planning, and costing exercise that in 2000 was finalized as the *Five-Year Development Plan*. A key objective of the plan is to shift from basic school rehabilitation and construction to improving educational quality and developing a modern technical and vocational education system.⁷⁸ Developing the Plan also required that the ministry begin putting in place the statistical, policy analysis and financial management capacities needed to set proper priorities and manage them efficiently.

4.24 The *intifada* has impacted the sector in many ways. It has interrupted the establishment of improved management practices and has generally set the implementation of the Plan back significantly. The ministry must once again focus on keeping schools running, under very testing circumstances, while also needing to find the resources to cope with a new intake of 53,000 students for 2001, and similar numbers for 2002 – all of this within a straitened financial environment.⁷⁹

4.25 The crisis has meant costly delays in donor commitments to capital financing and capacity building.⁸⁰ At the same time, over 400 schools, primarily in Hebron and the south of Gaza, representing 22 percent of the primary and secondary school stock,⁸¹ have been damaged

⁷⁷ In 1994 the total fertility rate was an average of 6.24 children per woman of child-bearing age for West Bank/Gaza, the rates being 7.4 for Gaza and 5.6 for West Bank (Table 6, *World Development Report, 1996*, and Palestinian Central Bureau of Statistics' *Demographic Survey in WBG, 1996*).

⁷⁸ "...in addition to maintaining the high access rates to basic education and to increasing secondary education enrolment rates, [the Five Year Plan] foresees important, well-focused and cost-effectively managed efforts in the areas of curriculum development, textbook development and production in-service as well as pre-service teacher training, pedagogical support to schools and impact assessment." MOE, November 2000.

⁷⁹ Capital needs to accommodate the intake (898 new classrooms for 2001/2 are estimated at c. US\$48 million (MOE). The capital expansion program has also been affected by the disruptions on the ground.

⁸⁰ Approximately US\$100 million in donor assistance was spent on educational infrastructure between 1994 and 1999, and the Five-Year Plan envisages donor commitments of a further \$45 million per annum, for a total of US\$225 million for the 2001-5 period.

⁸¹ According to the *Five-Year Plan* there are 1,800 schools in WBG, of which 1,400 are PA-managed.

by armed confrontation and in many cases evacuated for periods of time. The damage ranges from broken windows to the total destruction of a vocational school in Tulkarem (at an estimated replacement cost of some US\$1 million)

4.26 Physical damage to schools, restrictions on movements and other effects of closure have combined to reduce instructional time for thousands of students. PCBS reports that 60 percent of school children (who totaled 542,000 in 2001) were absent from schools for at least one day, with a median of 10 days. MOE estimated in May 2001 that between 9 and 45 days of instruction would need to be made up in West Bank schools, depending on area, while 14 would on average need to be made up in Gaza. These figures, of course, do not account for the enormous distraction factors at work throughout the *intifada*.

4.27 Research shows that one of the best predictors of student learning is time-on-task, a function of the number of classroom instructional hours and time spent on homework. In the first *intifada* UNICEF found that Palestinian strikes and Israeli closures caused students to lose a high average percent of the school year; these lost days meant that between 15 and 66 percent of the curriculum was not covered, depending on the days lost at individual schools. Results from the 1993 International Assessment of Education Progress (IAEP) hint at the adverse effects of lost instructional time on learning. Using the Jordanian curriculum, West Bank eighth graders tested poorly on the IAEP relative to Jordanian students. The performance difference is plausibly attributable to the cumulative effects of lost educational time.⁸² If the current crisis continues much longer, a new cohort of Palestinian children will be likewise affected.

Table 14: Estimates of Average Percentage of School Year Lost in the First *Intifada*⁸³

<i>Location</i>	<i>1987/88</i>	<i>1988/89</i>	<i>1989/90</i>	<i>1990/91</i>
Gaza	35	47	35	43
West Bank	75	50	50	35

4.28 **Services.** The top priority for education providers has been to minimize disruptions to schooling. In early 2001 the ministry established a Committee for Emergencies and worked closely with donors (via the Sector Working Group on Education, for which France is the shepherd) to prepare a US\$13 million *Action Plan for 2001-2002*, the main components of which were the establishment of an emergency fund to cover the ministry’s operating cost deficit (US\$3 million), the rehabilitation and protection of schools damaged or near flashpoints (US\$2.4 million), counseling and remedial education (US\$2.7 million) and first aid and fire equipment for schools (US\$4.7 million).⁸⁴ Working closely with UNRWA and school

⁸² Students in grades 1-4 are especially vulnerable to lost instructional time. They require consistent reinforcement as they acquire skills and are too young to have developed effective self-learning procedures. The eighth graders tested on the IAEP in June 1992 had just started the fourth grade when the first *intifada* began in late 1987. Although their learning would not be as vulnerable to school closures as those in grades 1-3, they still would not have had well-developed self-learning practices.

⁸³ *The Situation of Palestinian Children in the West Bank and Gaza Strip*, UNICEF West Bank and Gaza Strip, July 1992, p. 65.

⁸⁴ The *Action Plan* aims to maintain a developmental perspective during the emergency, stressing the need to “keep the educational process in good functioning order, at the minimum required levels of efficiency and equity, so that all children will be able to exercise their basic human right to education, stipulated and guaranteed by many international covenants to which all Governments of the region have committed themselves.”

communities, MOE has also decentralized authority to school districts to permit greater flexibility and cooperation between them without constant recourse to the ministry. Teachers and students have been redistributed across districts, volunteers and supervisors have stood in for absent teachers, and other ministries have been approached for transportation. The ministry has also used distance learning and has carried out compensatory/catch up teaching. These actions, necessitated by the emergency, have potentially important long-term benefits.

4.29 **Resources.** In addition to the financial implications of repairing physical damage, providers have had to absorb increased costs on account of emergency transportation and accommodation and the salaries of replacement teachers. MOE’s financial situation is, in a structural sense, more comfortable than that of MOH, in that school non-salary operating cost requirements are far less than those required to run the health system.⁸⁵ The original 2001 MOH budget for 2001, drawn up prior to the *intifada*, envisaged a 7 percent increase in salaries and it was intended to allow for this by a reduction in operating costs of 7 percent.

Table 15: Non-Salary Operating Costs for Schools, 2001

<i>Budget Category</i>	<i>Actual Expenditures 2000</i>	<i>Original 2001 Budget Allocation</i>	<i>Spending Plan Allocation (6 months)</i>	<i>Funds Received from MOH as of August 31, 2001</i>
Operating costs (official travel, rents, water, electricity, stationary, maintenance)	US\$7.88 million	US\$7.3 million	US\$3.2 million	US\$0.11 million

4.30 In the *Six Month Spending Plan* for April–September 2001 (para. 4.6), salaries were protected while operating costs were cut from the original figure of US\$7.3 million to US\$3.2 million (a cut of 44 percent). In practice, though, actual transfers from MOF amounted to only US\$110,000 between October 2000 and August 2001.⁸⁶ The Ministry has in effect been obliged to work without any provision for operating costs, and this has required the suspension of many “non-essential” programs (e.g. teacher and management training) as well as contracting debt to suppliers. Given the small sums involved in comparison to the total budget of the Ministry, this squeeze on operating costs seems neither necessary nor advisable, particularly in view of the fact that quality education is so dependent on the standard of teaching, and that good teaching requires constant training and inspection. The growing inability of students to pay fees has also impaired the schools’ ability to cover their regular running costs.⁸⁷

⁸⁵ For 2000, education sector operating costs represented only 4.6 percent of the sector budget, as opposed to 41 percent in health, and in absolute terms were only 22 percent of health operating costs. Salary expenditures amounted to 92-93 percent of the budget in each of 1999, 2000 and 2001 (original budget).

⁸⁶ The major items in the MOE *Spending Plan* operating cost budget are water and electricity (37 percent), communications (16 percent), transport (15 percent) and maintenance (11 percent). MOF *commitments* against budgeted items in the period total \$360,000, or some 11 percent of the approved emergency budget.

⁸⁷ Fees are paid and retained at the school level.

Universities

4.31 **The Sector.** University and college activities have also been badly affected, and are being run on a day-to-day basis to adjust to access and security problems and an increasing budgetary crisis. It is also reported that most foreign professors have returned to their home countries.⁸⁸ A certain amount of physical damage has also occurred – in particular to the Palestine Technical College at Khadouri, Tulkarem. The college was extensively damaged by shelling in November 2001, and replacement costs are estimated at US\$2.7 million.

4.32 **Resources.** Through the 1970s and 1980s, about three-quarters of the recurrent financing needs of the university system came from PLO resources, while most of the funds needed for construction were donated by expatriate Palestinians and charitable organizations. The influx of aid from PLO and philanthropic organizations contributed to the expansion of a system charging relatively low tuition charges (with only about 10 percent of the cost of educating a student recovered through fees). During the first *intifada*, tuition fees were waived, creating expectations that have persisted. The pattern of significant external funding and low tuition fees has now altered. In the early 1990s, contributions by the Gulf States to the PLO ceased and tuition fees as a share of total university income increased to around a third. In the middle of the decade, the EU provided recurrent cost support to ease the fiscal pressures on the universities, on the basis of an understanding that this support would gradually diminish over a five-year period. Although EU support has been phased out, self-sufficiency in the sector was never achieved.

4.33 On the outbreak of the *intifada*, 68 percent of the universities' recurrent budget came from fees, 10 percent from the PA, and another 12 percent from donors and other revenue sources.⁸⁹ Universities ran a chronic deficit of about 10 percent of total budget, and in some cases were drawing on staff pension funds as a stop-gap measure. Public funding was erratic and no clear strategy for addressing sector financing had been developed.⁹⁰ By 1999, average university fees amounted to 37 percent of average per capita GDP, meaning that universities have little or no scope to raise fees further, especially given current levels of unemployment. Those who can afford university education are, unexpectedly, the wealthier, and seeking full cost recovery will need to be done in such a way that the access of the poor to higher education is not blocked.

⁸⁸ Hossam Sharkawi, *Ibid.*

⁸⁹ As of 2000, the PA supported the Al-Quds Open University and the Al-Azhar University in Gaza. At the college level it supported the College of Education in Gaza and the Ibn Sina Nursing College in West Bank; at the community college level, the Palestine Technical College/Khadouri, the Palestine Technical College/Arroub, the Palestine Technical College/Ramallah, Ul Ummeh Community College in the West Bank, the College of Science and Technology and the Palestine Technical College/Deir Al Balah in Gaza.

⁹⁰ The Ministry of Higher Education (MOHE), with technical assistance from the World Bank, is currently developing a higher education financing strategy in order to help improve the management and efficiency of Palestinian higher education institutions, and to make better use of PA subventions.

Table 16: The Financing of Higher Education

<i>Higher Education Financing</i>	<i>1997</i>	<i>1999</i>
<i>Expenditures</i>		
PA (institutional, MOHE) (US\$, million)	12.5	10.4
Percent of PA budget	1.5	1.1
Percent of PA educational budget	7.7	5.9
Percent of total higher education expenditures	19.0	14.5
<i>Recurrent Expenditures per Student</i>		
University (US\$)	1,134	857
Community college (US\$)	1,071	993
<i>Institutions' Revenues and Sources</i>		
University revenues (US\$, million)	28.4	42.0
Community college revenues (US\$, million)	1.7	3.1
University tuition fees (US\$, million)	21.6	36.0
University tuition fees as percent of recurrent costs	42	68
University tuition fees as percent of university revenues	76	86
Average tuition fees per student	476	582
Average tuition fees per student as percent of GDP per capita	32	37

Source: Ministry of Higher Education and Scientific Research. "Developing a Strategy for Financing Palestinian Higher Education", July, 2001, Table 4.

4.34 In 1997-98 the university sector ran a deficit of US\$14 million.⁹¹ Since the crisis, institutions of higher learning estimate losses of US\$5-7 million per month in running costs, mainly owing to the inability of students to continue paying their fees as a result of growing unemployment and declining incomes in WBG, but also because of a suspension of PA subsidies. In addition, the universities report losses of about US\$8 million in planned capital contributions from fees (which in the event could not be drawn upon).⁹² Thus the current emergency has significantly deepened the pre-crisis deficits of these institutions, to the point where their continued operation through 2002 without emergency assistance is open to question. At present the university system does not receive any significant recurrent cost support from the donor community, though in 2001/2 the Ministry of Higher Education, with seed funding of US\$1.5 million from the Islamic Development Bank, launched a Student Revolving Loan Fund (SRLF); 8,400 students have benefited from this facility. For the current academic year, the Ministry is seeking a minimum additional US\$3.5 million to cover 14,500 students under the SRLF.

Social Assistance Delivery

4.35 The need for social/humanitarian assistance has risen steeply since October 2000. As of June 2001, some 74,200 households, or 14 percent of the total in WBG, were reported to have lost all their income, while up to 75 percent of the refugee population was thought to have fallen below the poverty line.⁹³ MOSA has estimated that 85,000 families are in urgent need of income

⁹¹ Source: Ministry of Higher Education.

⁹² Hossam Sharkawi, *The Impact of the Intifada on Health and Education*, August 2001.

⁹³ PCBS data.

support. With family size in WBG averaging 6.4, this represents 545,000 people, or 18 percent of the population.

4.36 **Services.** MOSA offers two main services – income support, and social centers/programs.

- *Income support* consists of cash, food and provision for medical treatment, with income support payments and food distribution the most important features.⁹⁴ Families eligible for cash support from MOSA include those with no male breadwinner at home (due to absence or incapacity to work), or with a total labor income inferior to a scale of assistance defined by the ministry. The cash assistance norm is adjusted up to account for family size, and/or reduced if the beneficiary is already receiving food support from UNRWA or the World Food Program. The average eligible family of ten members is entitled to receive around US\$1,290 per annum. In addition, depending on availability, MOSA distributes food provided it by the World Food Program. Despite the clear need for such assistance and the lack of adequate budgetary resources, donors have not provided significant contributions to this program, in part because of concerns about how assistance is targeted. The capacity of the ministry would undoubtedly be improved by a program providing support for the development of information and organization systems (for example, by linking the record systems of the ministry and its district centers, and maintaining full records of beneficiaries of non-MOSA income support (i.e. from the President’s Office, NGOs and UNRWA).
- *Social centers/programs.* MOSA’s 55 centers and programs offer several types of service, including physical rehabilitation, vocational training, and shelter for orphans and old people.⁹⁵ These centers have continued to be supported by donors such as Sweden, UNICEF (childcare activities including for orphans and early childhood programs), UNIFEM (skills development/vocational training for women) and the UAE (for a large physical rehabilitation center in Nablus).

4.37 **Resources.** MOSA’s operating costs are divided into two categories – the operations of the ministry’s staff and facilities, including its social centers, and the recurrent costs of the social assistance system.

Table 17: MOSA Non-Salary Operating Costs & Social Assistance, 2001

<i>Budget Category</i>	<i>Actual Expenditures 2000</i>	<i>2001 Budget Allocation</i>	<i>“Spent” to end-August (8 mths)</i>	<i>Funds Received from MOH as of August 31, 2001</i>
Operating costs (official)	US\$0.89 million	US\$0.82 million	US\$0.58 million	US\$0.33 million

⁹⁴ In May 2001, for instance, one third of the cash assistance paid out went to female-headed households; another third to households facing temporary difficulties (disease, family problems, housing problems etc), and one fourth to households where the head of household suffered from a permanent handicap. Four percent of beneficiaries were falling under the category “low income”. In collaboration with MOE, MOSA also provides some tuition support to students belonging to families with limited income.

⁹⁵ There are 21 houses for the elderly (which provide financial and medical assistance for 460 in-house cases as well as outside cases), 3 orphanages, 8 physical rehabilitation centers and 22 vocational training centers for school dropouts and youngsters with social adjustment issues.

travel, rents, water, electricity, stationary, maintenance)				
Social Welfare System recurrent costs	US\$42.2 million	US\$47 million	US\$28.2 million	US\$18.2 million

4.38 As indicated in the table above, MOSA had not as of August 31, 2001 received budgeted operating costs at the levels required, and little more was received during the rest of 2001 – to the extent that senior staff in Ramallah were paying utility bills from their own pocket by the end of 2001. This impacted on MOSA’s ability to operate its social centers and the programs run through them. More serious than this is the lack of funds for MOSA’s social assistance program. In 2000, MOSA received US\$42.2 million to support payments to 36,000 “social hardship” families.⁹⁶ As discussed earlier (para. 3.48), the number of the poor has more than doubled during the *intifada*, and in recognition of this trend MOSA’s social assistance budget was raised to US\$47 million for 2001, enough to provide for 45,000 families.⁹⁷ However, disbursements against this budget commitment have proven erratic and completely inadequate. As of the end of August 2001, only US\$18.2 million had been provided to the ministry for these hardship cases, and little was received thereafter. In January 2002, it was reported to the *Assessment* team that payments to the 45,000 registered families were seven months behind schedule and were being paid only one month in every three.

4.39 To the extent that families have received support in recent months, it would appear to have been channeled to those who have lost their jobs in Israel or whose homes and farms have been destroyed, and to families of the dead and injured -- often as direct transfers from the President’s Office or MOF. Most of the “unemployable poor” (widows, wives of prisoners, the disabled, elderly people and orphans) have been left with no means of PA support. As pointed out above, the clear need for emergency support has not evoked a corresponding response from donors, who have tended to channel such funding through UNRWA, as well as small sums through NGOs.

THE RESPONSE OF THE MUNICIPALITIES

4.40 **Services.** Municipalities reacted to the financial crisis of the *intifada* (paras. 3.31-3.35) slowly at first, and then more aggressively as they realized that the crisis was not likely to be resolved quickly. Some gave incentives (discounts) to consumers for the payment of bills. Others embarked on more determined revenue collection drives targeted specifically at those in the community who are able to pay. This yielded some dividends, but there were limits to this strategy. Eventually, all municipalities were forced to reduce expenditure. Some did so more quickly than others, and some more radically, with the timing and depth of the cuts dependent on specific local factors – the particular resource endowment, managerial capacities and political pressures.

⁹⁶ A further 25,000 refugee families (roughly 20 percent of the pre-*intifada* WBG poor) were supported by food and cash payments from UNRWA (paras. 4.46 ff).

⁹⁷ In addition to which, some 20,000 families are on MOSA’s waiting lists as it is not considered possible to further expand the register at this time.

4.41 Municipalities have commonly been forced to eliminate new projects, cut back on maintenance and reduce the level of services. In most cases there have not yet been significant staff lay-offs, though some non-essential and temporary staff have been made redundant. Many municipalities have had to delay salary payment or introduce salary cuts (of a varying number of days per month), and to reduce their funding of staff pensions. As an increasing number of municipalities are obliged to reduce employment and benefits, so protests from municipal labor have begun (e.g. in Bethlehem), and are expected to increase.

4.42 The status of municipal services can be summarized as follows.

- *Water services* have been relatively unaffected so far, though the maintenance of water systems is in decline and spares are running short. Two/three months of liabilities to the Israeli public supplier, Mekorot, are commonly outstanding in those municipalities receiving their water from Israel. *Wastewater services*, which have been somewhat neglected to this point anyway, do not appear to have deteriorated perceptibly, though fears of contamination are rising as maintenance is deferred.⁹⁸ The main Gaza wastewater treatment plant was damaged in mid-2001 and its capacity reduced. In villages, however, the story is different. Some 280 communities in WBG are currently unserved by piped water networks and require supply by tanker. Closure and the recourse to roundabout routes has affected the price of water significantly – a tank of 10 cubic meters, which used to cost NIS 120-140 prior to the *intifada*, may now cost as much as NIS 200.
- *Electricity*. Municipalities that rely on electricity to generate cash surpluses to fund other services (for example Nablus and Hebron) have been badly hit by the decline in electricity fee payments.⁹⁹ Most have responded by reducing electricity supply (for example, street-lighting).¹⁰⁰ In some areas (e.g. Hebron) transformers have been repeatedly damaged or destroyed by Israeli military action. With replacement generators difficult and costly to obtain, systems breakdowns are now common. In many municipalities there is a build up of 3-4 months of liabilities to the Israeli public supplier, with a decreasing capacity to clear the debt.
- *Solid waste collection and disposal* are deteriorating. This service embodies heavy recurrent costs on account of salaries & wages, fuel, and vehicle and equipment spares. Collection in many places is down from three or two shifts to one; garbage is piling up in the towns, and people are resorting to burning it in the streets. In addition, the transfer of garbage to dump sites has in many cases been blocked or interrupted by the Israeli army. This has forced some municipalities to create transfer stations near to residential areas. The potential public health problem is obvious.
- *Road maintenance*. Most municipalities have little money for maintaining local roads, and most such work done during the *intifada* has been funded by donors through job creation programs. This is likely to prove very costly if not remedied, since many of the

⁹⁸ The closure of most municipal slaughterhouses has led to more home butchering and to a significant increase in the amount of blood in the waste-water.

⁹⁹ No Gaza municipalities supply electricity.

¹⁰⁰ As well as cutting back other activities which depend on the cash surpluses, such as solid waste collection and road maintenance.

small roads in and around the municipalities have been over-trafficked due to the need to circumvent checkpoints.

Box 15: A Sample of Municipal Service Delivery Problems

Gaza City

Solid waste collection is a major problem, as there are insufficient funds to pay for the large staff and large vehicle fleet, a lack of spares, and shortages of funds to buy fuel. Pickup has been reduced from three times to once per day. To date, there has not been any significant lay-off of staff but benefits and pensions are not being fully funded.

Payment arrears to Israeli companies total \$2 million.

Rafah and Khan Younis

The income drop has been very sharp because of a high dependence by households on employment in Israel.

The financial burden on these municipalities has been increased by a need to deliver additional services to households affected by the conflict (including re-housing and emergency services). Some areas (e.g. Moraj) have been almost totally cut off from services on account of the military presence.

Building activity is much diminished, further reducing revenue from building licenses and permits.

Difficulties are being experienced in garbage collection generally, and disposal in the case of Khan Younis is problematic due to the problems of gaining access to dump sites.

Hebron

Particular problems are being experienced due to the division of the city into areas H1 & H2, with H2 under Israeli military control. Obtaining access to or egress from H2 is very difficult, and this severely hampers economic activity and service delivery.

Electricity transformers have been shot out, in large numbers and repeatedly, causing frequent disruptions to supply and reducing Hebron's transformer stock to near-zero. Electricity consumption and revenues are down. Street lights have been reprogrammed to reduce electricity usage.

There are major problems with solid waste collection due to lack of spares, fuel and salary budgets, and damage to containers from shooting. This has resulted in a build up of garbage in the city. The garbage disposal problem made worse by the difficulty in obtaining access to any dump site.

Water supply system maintenance has been reduced and problems with spares and pumps are increasingly frequent.

Nablus

The reduction in revenues is now endangering the municipality's ability to pay its staff and maintain basic services.

Electricity services have been reduced and power cuts are increasing. Transformers and other spares have become unaffordable.

Access to the landfill is being hampered by Israeli military road blocks, resulting in an increasing build-up of garbage in the city.

Spares for the water system are in very short supply.

4.43 **Resources.** As outlined in **Chapter 3**, most local governments experienced a sharp fall in their revenues, with losses in the *Assessment* sample ranging from 17 percent on average in the West Bank to about 30 percent in Gaza. Within each region, revenue losses vary greatly between different municipalities, reaching 50 percent in some Gaza municipalities. The pressure on the delivery of municipal services has consequently ranged from the manageable to the disastrous.

4.44 The West Bank municipalities sampled are five times better off in terms of average per capita annual revenues than those in Gaza (US\$215 versus US\$40).¹⁰¹ There are also important structural differences in the service profile in different municipalities. Most of those in Gaza do not supply electricity; this means that Gaza municipalities depend mainly on cash surpluses from water revenues to finance local services, particularly solid waste, road maintenance and wastewater. West Bank municipalities, on the other hand, depend on the cash surpluses from their electricity revenues. Some West Bank municipalities, notably those in the Jerusalem and Bethlehem districts, do not deliver either water or electricity services and rely instead on building permit fees to fund local services.

4.45 The decline in municipal revenue is taking two forms. Incomes have decreased because of job losses and the overall recession. This situation has been made considerably worse by armed confrontation and uncertainty about the future: with less income and greater uncertainty, many people by mid-2001 were withholding or reducing payments for service -- some because they could not afford to pay, and others because they wished to conserve their income against further hardships.

THE RESPONSE OF UNRWA

4.46 **Services.** UNRWA is the second-largest provider of social services (health, education, social welfare) in WBG after the PA, employing approximately 10,000 WBG-based staff. UNRWA used two main kinds of assistance to respond to the crisis: *food and cash assistance*, and *employment generation* programs.

Table 18: UNRWA Emergency Appeals, October 2000-December 2002

<i>Appeals</i>	<i>Period</i>	<i>Requested (US\$ million)</i>	<i>Confirmed Pledges (US\$ million)</i>	<i>Confirmed Pledges (%)</i>	<i>Surplus/Deficit (US\$ million)</i>
Flash	Oct 2000	4.9	1.7	34.7	-3.2
1 st	Nov 2000	39	44	112.8	5
2 nd	Mar-May 2001	37.19	24	64.5	-13.19
3 rd	Jun-Dec 2001	76.89	62.8	81.7	-14.09
4 th	Jan-Dec 2002	117.06	0.43	0.4	-116.63
Total Pledges to Date		275.04	132.93	48.3	-142.11

- *Food and Cash Assistance.* The first of UNRWA's main *intifada*-related emergency appeals (US\$39 million requested, US\$44 million raised) largely concentrated on food aid, with more than half of the resources raised used to provide basic food commodities and cash subsidies to 217,500 refugee families (90,500 in the West Bank and 127,000 in Gaza).¹⁰² In the West Bank, some 57 percent of the refugee families which had not previously received food assistance were provided it by UNRWA. Food assistance is

¹⁰¹ The *Assessment's* sample of municipalities (particularly in the West Bank) is biased towards the larger and wealthier ones. The situation in the smaller and less wealthy municipalities and village councils is significantly worse than this sample indicates.

¹⁰² Special hardship cases families, approximately 25,000 families, who are provided with food assistance under UNRWA's regular program, were excluded from the emergency food aid program.

generally supplied for three months, and is worth US\$75 per family per month (US\$35 in kind plus US\$40 in cash). Distribution lists of affected families have been drawn up by UNWRA with the help of the PA, which provides information on laborers who have previously held Israeli work permits. Information from grassroots organizations, camps committees and village councils is also taken into consideration. In addition, poor families have received lump-sum cash assistance from the *intifada* appeals averaging US\$350 (ranging from US\$100 to US\$1,000 depending on their situation). Beneficiary families are only selected after careful assessment by UNWRA’s network of social workers. In particular, families who lose their breadwinner and are deprived of any other assistance are selected as a matter of priority.

The Employment Generation Program. This program was developed to provide temporary jobs to unemployed refugees. About US\$8 million was allocated to employment from the resources raised by the first appeal. The second appeal (US\$37 million requested, US\$24 million raised) and the third appeal (US\$77 million requested, US\$63 million raised) gave much more prominence to job creation, with about 45 percent of total financial resources initially allocated to the objective of creating 1.2 million job opportunity days in 2001. A major advantage of job creation programs is that they are largely self-targeting, since they aim by definition at the unemployed poor who are able to work and agree to receive only US\$12 per day. Under the UNRWA jobs scheme, workers have also been selected on the basis of family size to ensure that the program reaches a significant number of beneficiaries, while the wage paid has been tailored to the poverty line of US\$2 per person per day, assuming an average family size of 6 members. Priority was also given to locating schemes in the poorest regions of southern Gaza and the southern and northern areas of the West Bank. UNRWA aimed to reserve 30 to 50 percent of the jobs for women in certain activities within the “direct hire” component of its program (60 percent of the jobs are managed by UNRWA, with the balance implemented by private contractors and communities).

Table 19: Planned Budget and Beneficiaries of UNWRA’s Emergency Appeals, November 2000 – May 2001

	<i>West Bank</i>	<i>Gaza</i>	<i>Total</i>
Food Aid (\$million)	12.6	20.4	33.0
Employment generation programs (\$million)	9.4	16.5	25.8
Selective cash assistance (\$million)	2.4	0.9	3.4
Other assistance (\$million)	5.4	8.8	14.2
Food Aid (families)	90,000	127,000	217,500
Employment generation programs (working days)	151,300	389,000	540,600
Selective cash assistance (families)	8,800	2,250	11,050

Source: UNRWA.

4.47 **Targeting.** UNRWA is commonly considered to have performed well during the crisis, and is not subject to the concerns expressed in some quarters about the way in which emergency assistance is targeted.¹⁰³ UNRWA’s regular programs have served to provide a systematic basis

¹⁰³ See, for example, OCHA – *Overview on Food and Cash Assistance, 2001*.

for identifying and monitoring those in need, and the same system has been used to cope with the *intifada*.

4.48 **Resources.** UNRWA's regular annual budget for 2000 for WBG is \$138 million,¹⁰⁴ in addition to the emergency appeals budget of \$275 million intended to cope with the demands of the *intifada*. UNRWA is funded by donors through regular meetings of its own Donor Group. In recent years, the agency has experienced difficulty in fully financing its regular programs, a situation that eased somewhat this year as donors saw the agency as an obvious channel for providing emergency assistance to WBG.¹⁰⁵ The four emergency appeals have so far raised US\$133 million, leaving a deficit of US\$142 million.

THE RESPONSE OF NGOS

4.49 NGOs have traditionally played an important role in Palestinian society, and account for a large proportion of health services, rehabilitation for the handicapped, preschool education and agricultural extension and land rehabilitation. In the early 1990s, NGOs were receiving an average annual amount of perhaps US\$120-180 million in official donor/INGO assistance.¹⁰⁶ This had fallen to about US\$52 million by 1999.¹⁰⁷ In addition to this, measured private flows to "Islamic" NGOs appear to have amounted to at least US\$35 million by 1999, though this is thought by many to understate real flows quite considerably.¹⁰⁸

¹⁰⁴ Part of a US\$405 million budget (2001) that covers all UNRWA operations in WBG and elsewhere in the region, consisting of US\$311 million for operating costs, US\$65 million for O&M and US\$30 million for food commodities. Of this, US\$285 million for operating costs, US\$20 million for O&M and US\$30 million in commodities have thus far (as of end 2001) been financed.

¹⁰⁵ Operating in a climate of constant funding shortages has meant, though, that UNRWA was not able to increase salaries between 1995 until this year, which has resulted in an erosion of pay of 40 percent in relation to UNRWA's comparators.

¹⁰⁶ World Bank, *Memorandum of the President for the Palestinian NGO Project, 1997*.

¹⁰⁷ In 1999, according to a *Survey of the Palestinian NGO Sector* by the Palestinian Economic Policy and Research Institute (MAS), NGOs were thought to have received a total of about US\$52 million from Consultative Group donors, accounting for some 47 percent of the total of US\$112 million resources available to NGOs, followed by contributions from non-official donors (29 percent) and from local donors (11 percent). Almost all surveys of NGO activity point to lack of funding as a primary constraint to further expansion of NGO work in the West Bank and Gaza. In MAS' 1999 survey, 52% of NGOs interviewed claimed to suffer chronic budget deficits.

¹⁰⁸ For example, the Ministry of NGO Affairs estimates pre-*intifada* fund flow to "Islamic" NGOs at some US\$200 million per annum.

Table 20: A Profile of Palestinian NGOs in WBG (1999)

<ul style="list-style-type: none">➤ Total number of active NGOs in WB and Gaza: 926.➤ Geographic distribution: 76% headquartered in the West Bank, 23% in Gaza.➤ Concentration: 60% of organizations focus on urban areas, 29% on rural areas and 11% on refugee camps.➤ NGOs work in the following areas/sectors: 56% on scientific and cultural projects; 40% on child services; 35% on education; 33% on charitable work; 30% on youth; 26% on vocational training and rehabilitation; and 26% on health.➤ Typology: 40% are charitable organizations; 30% are youth clubs; and 29% are “new” NGOs (more developmental focus).➤ 96% of NGOs are registered with one of the following: Ministry of Internal Affairs, Ministry of NGO Affairs and Line Ministries.➤ Registration with line ministries covers 81% of NGOs, registration with the Ministry of NGO Affairs covers 10%.➤ 56% of NGOs in Gaza and 32% of NGOs in the West Bank were established after the PA.➤ While most NGOs rely on more than one source of funding, 78% of them rely on one source for more than 50% of their budget.➤ 39% of NGOs rely on private funds as their main source of revenue, and 19% on donor financing.➤ A huge disparity exists in the amount of funding available to NGOs. In 1999, the total amount of funding was US\$112 million, with an average of US\$160,000 per NGO. One NGO alone had an annual revenue of US\$12 million.➤ In 1999, 52% of NGOs faced a financial deficit.➤ NGOs in the central West Bank, representing 26% of the total number of NGOs, receive 60% of the resources available.➤ The average per capita assistance received from NGO resources in the West Bank is US\$12 while it is only US\$2 in Gaza. It is highest in the southern areas of the West Bank.

Sources: Palestinian Economic Policy and Research Institute (MAS).

4.50 Services. With increasing levels of hardship, NGOs have again stepped forward to provide essential services, much as in the first *intifada*. They have played a prominent part in providing health services and supporting farmers who have lost land, capital or market access. NGOs have also been used by donors to channel in-kind and cash assistance to the poor and to the families of those killed and injured. Another area where NGOs have played an effective and growing role is in employment generation, where they have been able to initiate income generation activities among the poor. Following a successful US\$1 million pilot in early 2001, donors have committed a further US\$6 million to NGO job creation projects through the World Bank’s Palestinian NGO Project. USAID has recently committed a further US\$10 million to similar programs. NGOs have also provided support on a contractual basis to MOH for psychological counseling and rehabilitation.

Box 16: Job Creation and NGOs – the Palestinian NGO Project

In December, 2000 the World Bank earmarked a total of US\$1 million from the *Emergency Response Project* for job creation projects to be managed by NGOs.

This fund was managed by the Welfare Association Consortium (WAC), established in 1995 as the administrator of the World Bank-financed *Palestinian NGO Project*, which gives grants to NGOs for the delivery of basic social services. Through the local media, WAC solicited proposals for emergency funding and set up an ad hoc committee consisting of NGO and PA representatives to select projects according to agreed criteria. WAC's supervision and auditing standards were then applied during implementation. By February, WAC had approved 33 projects, 12 in Gaza and 21 for the West Bank, ranging from US\$10,000 to US\$100,000, with the larger grants going towards job creation projects in the agricultural sector. To compliment the main focus the *Emergency Response Program* on urban infrastructure and public works, grants to NGOs were concentrated on health, education, agriculture, pre-education, youth and community services with priority given to projects that benefited the most disadvantaged of the community, including women, children, youth and people with special needs.

By June 2001, the US\$1 million had been disbursed, generating 54,000 labor days and with an overall sub-project labor content of 68 percent.

The following is a sample of projects and their achievements.

- *The Palestine Hydrology Group* rehabilitated 40 wells with a total of US\$50,000 generating 2,000 workdays.
- *The Kufur Ra'i Sports Club* re-developed a 6-dunum football field generating 400 workdays for a total of US\$9,000.
- *The Mercy Association* rehabilitated 16 houses of indigent families in Gaza generating a total of 1,640 workdays for a total of US\$40,000.
- *Al-Bait Al-Samed* in Gaza produced 6,000 pieces of garments, half of which were distributed to the poor and the rest of which were sold to generate income for the NGO. 1,800 women workdays were generated for a total of US\$30,000.
- *Al-Tawfeek Cooperative for Fisherman* provided 1,200 kg. of material that was used by fishermen to make fishing nets to replace those lost as a result of fisherman not being allowed to fish, leaving their nets in the water. The project generated 3,000 workdays at a cost of US\$48,000.
- *The General Union of Palestinian Women* treated 232 children suffering from psychological stress, transferring 42 severe cases to special units. The project generated 2,000 workdays for a total of US\$20,000.

4.51 Most of the 53 NGOs surveyed for the *Assessment* (70 percent) indicated that they have introduced new activities to cater to the emergency, despite financial difficulties faced (para. 4.52). At the same time, only 28 percent of those surveyed said they had been obliged to discontinue ongoing services, and in many cases these were not core services. Most NGOs coped with increased demands through longer staff hours. All of them faced difficulties in carrying out their programs – with 69 percent citing road blocks and closures as the main constraint to reaching clients. Given the already skewed concentration of NGOs in urban areas as compared with rural areas and camps (60 percent, 29 percent and 11 percent respectively),¹⁰⁹ this has further isolated the poor and marginalized in the more remote communities.

¹⁰⁹ MAS, *ibid.*

Box 17: Two Large Palestinian NGOs – PARC and UPMRC

PARC

The Palestinian Agricultural Relief Committees (PARC) has for many years played a pioneering role in providing development services in the agricultural sector and rural areas. Like other NGOs, over the past 13 months PARC had to modify its project delivery methods to adapt to closure and rising poverty and unemployment. A key element in their effort has been their decentralized management structure, with field offices in many districts of the West Bank and Gaza. PARC raised an extra US\$3 million to implement emergency projects focusing on income-generation and job-creation. Job-creation projects have concentrated on maintaining and developing agricultural resources (i.e. agricultural road construction, retaining wall construction, rehabilitation of cisterns and wells), with a particular emphasis on water. Additionally, PARC is promoting the household economy by supporting backyard gardens. These gardens provide their owners with a sustainable food source as well as the potential to earn extra income. Some of PARC's results in the *intifada* are:

- Creation of 40,000-50,000 job opportunities
- Construction of 100,000 m² of terraces
- Reclamation of 1,100 dunums
- Planting of 300,000 seedlings of fruits and vegetables
- More than 100,000 m³ of water harvested
- More than 180 km of access roads constructed.

UPMRC

In the first days of the *intifada*, The Union of Palestinian Medical Relief Committees (UPMRC) sought to ensure that basic medical services would continue to be provided in a situation of mounting violence. It relied on its large pool of First Aid Volunteers, assisted by health professionals and established field hospitals and First Aid Centers near confrontation sites. Later, responding to the increased pressure of closures, UPMRC organized eight mobile clinics to reach 1,500 patients a day and provide free services in areas under tight closure or curfew. UPMRC's efforts are currently directed at preparing people and communities to solve their health and development problems arising from prolonged closure. For example, UPMRC's Woman's Health Program distributes delivery kits and trains community health workers to assist pregnant women and to ensure they are not left on their own during labor. UPMRC has also developed comprehensive first aid training programs to ensure there are enough individuals throughout the West Bank and Gaza capable of handling emergencies and saving lives, and offers such training to schools and community institutions. UPMRC's health centers and Community Based Rehabilitation Program provide free medical and rehabilitation services (inc. home visits), and it has established loan centers to provide the injured with devices such as crutches and wheelchairs. In addition, UPMRC is providing support to a number of impoverished communities through its Small Community Projects Program (in which small-scale construction projects in villages and refugee camps provide work for the unemployed).

4.52 **Resources.** No figure is available on the total amount of additional funding made available to NGOs during the *intifada*, and any estimates must be treated with great caution. Nonetheless, it is evident that a number of NGOs have been able to tap new external resources.¹¹⁰ Estimates made for the *Assessment* suggest that official donor/INGO resource flows to NGOs may have totaled some US\$80 million in 2001, with external private flows to "Islamic" NGOs providing an additional US\$100 million. Despite this, the survey of NGOs conducted for the *Assessment* confirmed that many were ill-equipped financially to respond to the increase in demand for their services (particularly in welfare and health), and are now very short of funding for their regular/developmental programs. The survey also indicates that 60 percent of the sample had received at least 30 percent *less* funding during the *intifada*. In part this is due to steep losses

¹¹⁰ For example, UNICEF supported programs targeted at children in crisis, in collaboration with MOSA. Sweden and Switzerland supported health awareness, Japan worked through the Palestinian Agricultural Relief Committees on emergency projects in agriculture, while CIDA provided funding for programs in maternal and child health and Save the Children channeled emergency funds in a number of areas.

in service charges and local contributions – up to 60 percent in the case of the former. Those NGOs that received *additional* funding from donors tended to be the larger and better-established NGOs like PARC, the Palestinian Red Crescent and UPMRC. These professional NGOs continue to have a higher capacity to attract funding, while their service coverage is greater than that of the smaller NGOs. The funding situation and its impact on the social safety net – particularly insofar as *non-emergency* services are concerned – is clearly severe, however. A new element in the equation is the PA's recent decision to close or limit the activities of NGOs affiliated with *Hamas*.

Box 18: The Response of US Catholic Relief Services to the Crisis

Program title: Job Creation

Total intervention: US\$4.3m (WB US\$1.8m, Gaza US\$2.5)

Job opportunities created: 138,000 (labor content in WB 67% and in Gaza 35%)

Total beneficiaries: 10,000 families

Source of funding: USAID (82% of funds)+ Others

Sectors: agriculture (land reclamation, rehabilitation of agricultural roads); education (construction of kindergartens and community centers) and water (rainwater catchments for agricultural and drinking water purposes)

Geographical distribution: Jenin, Hebron, Gaza Strip

Implementation mechanism: direct implementation with local NGOs in coordination with Ministry of Local Government and other line ministries

Achievements: *in the West Bank:* 1,100 dunums of land reclamation, 190 rainwater catchments for agricultural purposes, 305 rainwater catchments for drinking purposes; *in Gaza:* 50 km rehabilitation of agricultural roads, 335 rainwater catchments for agricultural purposes, 1440m² construction of kindergartens and community centers, 1800m² rehabilitation of kindergartens and community centers.

Source: CRS.

THE RESPONSE OF THE DONORS

4.53 The *intifada* came as a shock to the donor system. The collective response from donors, however, has been timely, flexible and generous, even as donors have struggled with how they can adapt. Resources for budget support, job creation and other forms of emergency assistance have helped sustain the PA as a functioning entity and have mitigated the hardships suffered by the population. In essence, the donors have cushioned the Palestinian people, while helping preserve a governance structure for the future. At the same time, however, the medium-term agenda of sustainable development and institution-building has been partially compromised, reflecting the difficulty of persisting with these activities under closure and insecurity.

4.54 **The Quantity and Composition of Donor Assistance.** Data on donor flows has decayed during the *intifada*, making comparisons with periods prior to the crisis difficult.¹¹¹ **Commitments** appear to have increased sharply during the *intifada*, from US\$692 million in 1999 to US\$973 million in 2000 to US\$1,228 million in 2001. The increase is primarily due to an infusion of external budgetary support for the PA.

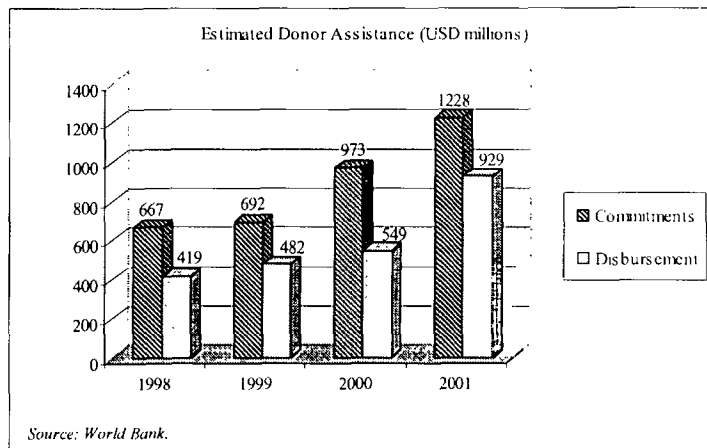
¹¹¹ MOPIC's quarterly matrix on aid flows does not capture data about informal assistance channeled through charitable organizations and individual donations, nor has its quarterly monitoring been able to provide comprehensive coverage of formal flows during the crisis. Data reported here is compiled from a combination of MoPIC's quarterly matrix, surveys conducted by UNSCO and the World Bank, and staff estimates, though its integrity is questionable and needs revisiting.

4.55 While data on *disbursements* must be treated with caution, these appear to have risen from US\$482 million in 1999 to US\$549 million in 2000 and US\$929 million in 2001. For 2001, 70% of disbursement was on budgetary support and emergency funding. Over the fifteen months of the *intifada*, donor total disbursements had exceeded US\$1.1 billion.

4.56 Several observations are in order. First, there has been a *shift in the source of major contributions*. The Arab League has become a major new player. At Arab League summits in October 2000 and later in March 2001, Arab donors pledged increased assistance to the Palestinian people and institutions, to be channeled through the Islamic Development Bank (IDB). Initially intended primarily for emergency and development projects, these funds have now been directed mostly to budget support, as well as to job creation activities and various development projects. By the end of December 2001, thirteen Arab governments had transferred to the IDB US\$672 million of

US\$693 million committed during the crisis. Of this amount, the IDB has committed US\$638 million and by December 31, 2001 had disbursed US\$448 million (amounting to over 40 percent of the total disbursed by donors during the first 15 months of *intifada*). The Arab League joined the two largest donors in recent years, the European Union and the United States, in contributing the lion’s share of commitments and disbursements for 2001 between them. The European Union¹¹² also stepped up its assistance during the period, has committed over US\$400 million since the beginning of the *intifada*, and had disbursed over US\$300 million of this by the end of December 2001, US\$245 of it in 2001. EU disbursements represented 26 percent of the total for 2001, a doubling of previous annual disbursements.

Figure 13: Donor Funding, 1998-2001



committed over US\$400 million since the beginning of the *intifada*, and had disbursed over US\$300 million of this by the end of December 2001, US\$245 of it in 2001. EU disbursements represented 26 percent of the total for 2001, a doubling of previous annual disbursements.

Table 21: The Arab League, the European Union and the United States, 2001 (US\$ million)

2001	Commitments	Percentage	Disbursements	Percentage
Donor Total	1228		929	
Arab League through IDB*	577	47	388	42
European Union (Bilateral & through	304	25	245	26
USA	242	20	114	12
	1123	92	747	80

* These figures do not include bilateral Arab support

** EU figures do not include support to UNRWA (some \$200 million committed in 2001)

¹¹² Including bilateral EU member states support and multilateral European Commission support.

**Box 19: Islamic Development Bank
Commitments and Disbursements during the *Intifada* (US\$ million)**

After the Arab League Summit in October 2000, two funds were established at the Islamic Development Bank: the Jerusalem *Intifada* Fund and the Al Aqsa Fund. A total of US\$1 billion was pledged in principle to these funds. Figures provided were current as of end-2001.

Jerusalem Intifada Fund

Support for *intifada*-injured and for families with *intifada*-injured or killed; educational and health support; emergency services.

Committed: US\$52.2 million. Disbursed: US\$17.8 million

Al Aqsa Fund

Support for PA budget.

Committed US\$405 million. Disbursed: US\$405 million.

Support for agriculture, health, education, roads, house and building rehabilitation, job creation, small and medium enterprises.

Committed: US\$131.4 million. Disbursed: US\$19.1 million

Joint (two-fund) Projects

Support for house and building rehabilitation, hospitals and clinics, export promotion.

Committed: US\$49 million Disbursed: US\$6.4 million.

Totals

Committed (by IDB): US\$637.6 million. Disbursed: US \$448.3 million

Committed (by participating countries): US\$693 million. Disbursed (to IDB): US\$672.2 million

4.57 Second, there have been *shifts in the composition of assistance*. After recent years in which donors and the PA had been able to focus more squarely on a range of longer-term social and economic priorities, the *intifada* compelled a return to precisely the kind of emergency programs that characterized assistance in earlier years of the peace process (recurrent budget support, employment generation). Out of US\$440 million disbursed between October 2000 and July 2001, 74 percent (US\$326 million) supported the PA budget, approximately US\$60 million was used for emergency programs (job creation, emergency health and welfare), and only some US\$36 million, or 8 percent, was directed to projects with a medium-term capacity building or infrastructure emphasis. This imbalance improved somewhat in the latter part of 2001, such that for 2001 as a whole some US\$175 million (19 percent of total 2001 disbursements) were allocated to medium-term developmental activities. While a necessary adaptation to the crisis, this shift in donor expenditure represents the displacement of long-term investment by short-term consumption, with a consequent loss in future growth. It is fortunate that the increase in donor disbursements meant that not all of the emergency expenditure came at the expense of growth-oriented investments. One unanticipated benefit of the renewed provision of budget support also needs to be mentioned. For the first time, a virtual freeze on public sector recruitment has occurred, thanks to the “hard” budget developed by MOF with the IMF. This has been reinforced by agreements between the PA and the EU in the context of EU budget support¹¹³ -- leading to agreements, for the first time, to contain public sector recruitment (stable since the second

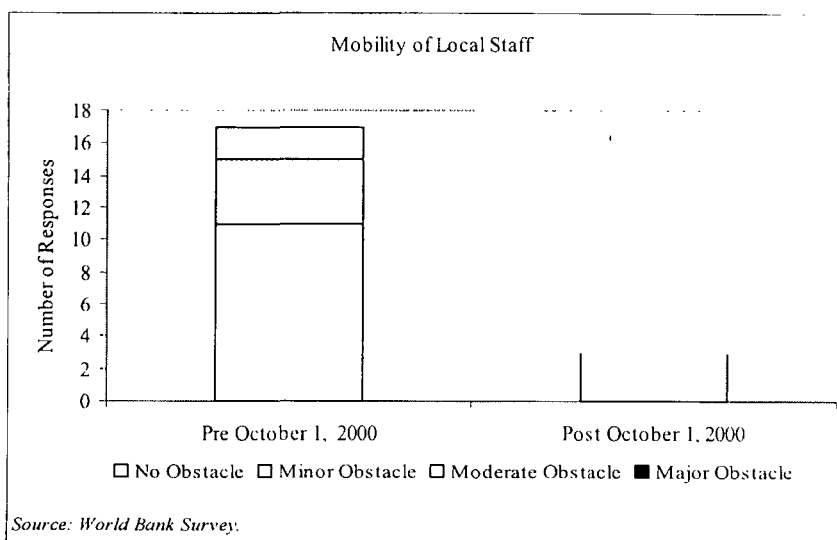
¹¹³ This totals 150 million Euros since the beginning of the *intifada*. MOF agreed with the EU and IMF in April 2001 on a program to implement measures designed to support transparency and sound fiscal policy. These included a) maintaining the consolidation of fiscal accounts under a single treasury account managed by MOF; b) a payroll freeze, followed by managed expansion only; c) the full transfer of responsibility for the payroll from the General Personnel Council to MOF in order to separate its administration from its financing; and d) the initiation, with World Bank technical assistance, of steps to unify and reform existing public sector pension systems.

quarter of 2001 with the exception of some necessary recruitment of teachers and health personnel in the third and fourth quarters), and to observe a fixed budget ceiling.

4.58 Impediments Faced by Donors.¹¹⁴ The crisis has imposed a series of new, or intensified, impediments on donor activities, stemming initially from restrictions on the *movement* of personnel and project inputs, and latterly from *damage to donor projects* by the Israeli armed forces.

4.59 Mobility. Many international consultants and contractors either left the area early in the *intifada*, or have been dissuaded from taking up new assignments; in particular, this affected the implementation of, and donor commitment to, large new infrastructure projects (cases in point being work on the Gaza Airport and Seaport). Gaza-based projects have been particularly hard hit as most international staff are prohibited from residing there and are thus obliged to commute, an inefficient and costly process. With limits on the use of international personnel, donors are even more reliant on Palestinian staff and contractors on whom the restrictions have been far worse, particularly getting in and out of Gaza. This has led to patchy supervision of projects, with a probable loss of quality in the donor portfolio. By the same token, local counterpart mobility -- both PA and contractor -- has been dramatically curtailed. In relation to goods and supplies, many donors report reduced or delayed availability of goods and raw materials, significant delays moving goods across internal and external borders, a consequently appreciable increase in costs (including a likely rise in contractor claims) and an overall slowdown in project implementation. In an environment already characterized by high transaction costs, donors estimate an average increase in project costs of some 15 percent.¹¹⁵

Figure 14: Mobility of Palestinian Staff of Donor Agencies



¹¹⁴ This section draws on material compiled by the Task Force on Project Implementation (comprising the European Commission, USAID, the World Bank and UNSCO), and a survey conducted of donors for the *Assessment*.

¹¹⁵ These increases were related largely to measures to protect staff security, transport costs and delays. In locational terms, Gaza and Hebron witnessed the highest cost increases.

Box 20: Implementing the World Bank Program During the Intifada

Over the years, the World Bank's West Bank Gaza program has shown strong performance. Four projects (the *Housing Project*, the *Microenterprise Project*, the *Legal Development Project*, and the *NGO Project*) have received superior supervision ratings by the Bank's Quality Assurance Group. In addition, the WBG portfolio disbursement ratios¹¹⁶ of 28 percent in FY00 and 26 percent in FY01 have both well exceeded the Middle East and North Africa Region and Bank-wide averages of 17.5 percent and 19.8 percent in FY00 and 14.6 percent and 20.5 percent in FY01 respectively. For the sixth year in a row, the satisfactory project audit rate in FY00 was 100 percent across the portfolio.

The current crisis has brought special difficulties. Several appraisal and supervision missions by HQ-based staff have had to be postponed, though implementation delays have been reduced somewhat by the use of video and teleconferencing.¹¹⁷ The responsibility of in-country staff has also been increased. Despite these adjustments, constraints on planning and carrying out project work have affected the speed and the quality of portfolio implementation. The projects least impacted by the crisis are those of a small-scale nature with strong community-driven dimensions, such as the two *Community Development Projects*, the two *Palestinian NGO Projects* and the *Emergency Response Program*. Their continued success is reflected in an ability to respond to community-identified needs and a reliance on community involvement in implementation, which translates in turn into satisfactory disbursement rates. Nonetheless, due in large measure to sustained dedication by strong counterparts and international consultants prepared to remain in place, the larger infrastructure projects in water (*Gaza Water and Sanitation*), electricity (*Electricity Sector Management Project*) and solid waste (*Solid Waste and Environmental Management Program*) have continued to perform well.

Bank internal reviews have identified the following factors as contributing to continued portfolio success under today's conditions. Interestingly, they are the same factors that tend to assure good performance under more normal conditions.

- Simple and clear project concept and design, including maximum flexibility
- Streamlined procurement and disbursement arrangements
- Counterpart agency capacity to implement, coupled with decentralized management to enable interventions across broad geographical areas
- Consultants and contractors with a track record of achievement and good results despite the challenging conditions
- Partnerships with other donors to leverage and diversify project financing/funding options
- Solid upstream project preparation to prepare for the implementation phase

4.60 *Damage*. Since the middle of 2001, damage to donor-financed projects as a result of Israeli action has increased, with certain facilities targeted by the Israeli Defense Forces. Notable among these actions was the destruction of buildings and the runway at the Gaza Airport (estimated at 9.3 million Euros by the EU), damage to the Palestinian Central Bureau of Statistics in Ramallah and the bulldozing of the Gaza Port contractor's buildings and equipment.¹¹⁸ Donors have also had to find ways to adapt to closure and the myriad of impediments it poses. Some have shifted to smaller projects with simpler designs and greater reliance on local technical expertise and materials. Others have increasingly decentralized their approach, relying on greater involvement of local governments and NGOs in project selection,

¹¹⁶ The disbursement ratio measures disbursements in a particular period as a proportion of total undisbursed commitments.

¹¹⁷ The recent negotiations for the *Emergency Services Support Project* were conducted from Washington by phone.

¹¹⁸ On February 4, 2002 the Spanish Foreign Minister, on behalf of the EU Presidency, wrote to Israeli Foreign Minister Shimon Peres expressing the EU's serious concerns at such destruction to its projects, which it estimated at US\$14.7 million, and reserving the right to seek compensation.

design and supervision. Those donors who continued to depend heavily on international experts and companies for implementation faced serious delays and, in some cases, termination of activity. This has in turn increased project costs substantially, including through claims of *force majeure*.

4.61 Types of Emergency Assistance and their Effectiveness Donor-funded emergency assistance took a number of forms, and was delivered through the PA, municipalities, various NGOs and UNRWA. Four types of emergency assistance are examined here, and certain omissions in the emergency effort are then identified.

4.62 Budget support. Although not primarily so designed, budget support has amounted to the largest of the emergency employment schemes, and the most significant tool for pre-emptive hardship alleviation.¹¹⁹ About three-quarters of the last year's PA salary bill has been covered by donor funds. Without this help, the 122,000 central government employees (about 25 percent of those currently employed in WBG, excluding East Jerusalem) could not have been paid. In addition, the liquidity injected into the local economy through the PA helped preserve domestic private economic activity, even if the multiplier effect was relatively muted by the enormous degree of leakage from the Palestinian economy.¹²⁰ The implication of concentrating assistance on salaries, however, has put additional pressure on government operating costs, as previously noted.

4.63 Food and cash assistance. Donor contributions to food and cash assistance increased with the *intifada*, in particular through UNRWA for the refugee population, and through NGOs for the newly unemployed and the families of those whose relatives have been killed or injured. It is estimated that some US\$70-80 million has been disbursed for this purpose.¹²¹ This has not been sufficient to offset the decline in PA funding for MOSA's social assistance programs over the period, let alone cater to the major increase in the incidence of poverty. In particular, the *previously* unemployed poor remained without additional assistance, and in many cases have lost benefits they were receiving prior to the *intifada* (para. 4.36). In addition to official donor contributions, though, at least US\$50 million in cash has been sent from private and governmental sources in the Middle East directly to the families of the dead and injured.

4.64 A key issue for donors is whether sound mechanisms for targeting such assistance exist, and this has inhibited additional donor contributions. Under more favorable circumstances, appropriate information could be derived from tax records or comprehensive household income surveys. The absence of such systems has left many local relief committees and NGO providers with the complex and controversial job of developing criteria for selecting who should receive the inadequate amounts of cash and food available. The list-based distribution mechanisms used

¹¹⁹ The Fafo village and town case studies cited in **Chapter 3** (*Paying a Price: Coping with Closure in Two Palestinian Villages; Paying a Price: Coping with Closure in Gaza City; Paying a Price: Coping with Closure in Jericho*, Fafo, Norway, 2001) indicate that access to a public sector salary has been the single most important social safety measure under present conditions. These results reinforce the findings of a World Bank study, which showed that job creation in the public sector in the years 1996-1998 had a significant and positive short-run impact on poverty alleviation, particularly in Gaza. By a similar token, one would assume that preserving civil service jobs prevented further increases in poverty.

¹²⁰ Whereby US\$1 spent in WBG on average delivers US\$0.75 cents to the Israeli economy, directly or indirectly (World Bank staff estimates).

¹²¹ Excluding UNRWA's regular program.

by UNRWA and the Ministry of Social Affairs provide models that could be adopted universally.

- *Food.* The provision of emergency food in WBG is controversial. Households interviewed on the subject for the *Assessment* consistently voiced discontent at the “humiliation” of having to claim food packages from distribution centers. Concern has also been raised about the appropriateness and nutritional value of food baskets, which lack protein and certain vitamins.¹²² Timeliness of supply is also an issue.¹²³ In addition, the appropriateness of providing food in a context where there is no generalized food shortage is questionable. The provision of food assistance has detrimental impact on local food production by forcing substitution of Palestinian products by food commodities procured abroad, though its overall impact on the economy appears positive.

Box 21: The Macroeconomic Impact of Food Aid

Food assistance has been an important source of hardship relief since the beginning of the crisis. It is estimated that a total of some US\$30-40 million had already been disbursed by June 2001, with most commodities (rice, flour and oil) purchased abroad. This amount, equivalent to approximately 3 to 5 percent of annual household food consumption in WBG, is large enough to generate significant macro-economic impacts. Counterfactual simulations run with the World Bank’s quantitative model suggest a negative impact on Palestinian food production and distribution, with an induced decrease in *sectoral* GDP of between US\$10-20 million (or the equivalent of 25 to 50 percent of total GDP losses in the sector). The impact of food assistance on prices appears to have been negligible, with most of the observed decline resulting from the impediments to distribution caused by closure. Since basic food consumption is relatively price- and income-inelastic, food donations encourage households to use the income thus saved to consume non-food products. The demand for Palestinian food products (and for imported food products sold domestically) therefore declines, but is more than compensated at the macro level by an increase in the demand for other products. In net terms, it is estimated that total GDP may have increased by US\$3-5 million as the result of an injection of US\$30- 40 million of food assistance in the Palestinian economy.

- *Cash.* Cash assistance is unpopular among aid administrators, as it suffers from the same targeting problems as food and is more readily misappropriated. Although a significant number of organizations, particularly community-based organizations like the Salah Islamic Organization and the Zakat Committees, have been providing regular cash assistance in WBG, targeting and distribution mechanisms are ad hoc and individualized. Once again, UNRWA’s reputation in this area is good. It is worth noting, however, that in the absence of general food shortage, cash assistance presents advantages over food by providing more flexible support to the beneficiaries (and hence more welfare-enhancing) as well as a better contribution to domestic markets. There is a clear case to provide support to MOSA to help finance the c. US\$20 million in arrears to the 45,000 hardship

¹²² MOSA food baskets foresee the distribution of flour and oil, but oil has often been unavailable (OCHA’s *Overview on Food & Cash Assistance*, August 2001). The compositional concern is important given the commonplace finding that the first component to be cut from the diet of those families experiencing financial hardship is meat.

¹²³ A significant factor is the irregularity of funds for food purchase, a problem also faced by UNRWA. Nor is the timely entry of foodstuffs guaranteed, and delays occur at marine ports and entrances to the West Bank and Gaza. These delays have often been long enough to cause spoilage of the goods in question.

cases on the MOSA register, and a proposal for a more ambitious Unemployment Benefit Fund is discussed in **Chapter 5**.

4.65 *Employment Programs.* As of October 2001, a total of US\$104 million had been committed by donors for emergency job creation, of which about US\$48 million had been disbursed, creating nearly 0.9 million work-days.¹²⁴ In total, the objective was to create some 2 million job-days once commitments were fully disbursed.

Table 22: Job Creation Programs (as of end-October 2001; excludes UNRWA)

<i>Donors</i>	<i>Commitments (\$ million)</i>	<i>Donors</i>	<i>Commitments (\$ million)</i>
Canada	3.2	Norway	7.9
Denmark	3.5	Spain	0.5
France	6.3	Sweden	5.0
Germany	12.6	Switzerland	0.2
ILO	0.6	United States	17.3
Islamic Development Bank	22.4	United Kingdom	2.2
Italy	0.7	World Bank	17.3
Japan	4.1	Other	0.15
Total		104.0	

Source: UNSCO (2001).

4.66 The primary objective of such programs is to relieve economic hardship by creating temporary jobs, and to do so in a way which avoids the targeting problems associated with food and cash assistance. By offering short term contracts and low wages, these interventions aim to reach the poor unemployed who may not have benefited from any other program of assistance. A second objective is to support Palestinian development goals by financing health, education and infrastructure projects.

4.67 Employment generation programs developed and implemented under the *intifada* were reviewed in October 2001 at two workshops convened by the World Bank in Ramallah and Gaza for the PA, donors and international agencies. The employment programs implemented in WBG are generally characterized by flexibility, fast disbursement, small size, and reliance on local private contractors. Procurement rules have been simplified and procedures decentralized, with an increasing trend toward consultation with municipalities and village councils on the choice/design of projects. Some donors have also allocated funds on a geographical basis, according to the extent of local poverty and unemployment (under closure, accurate geographical targeting is particularly important because of the restrictions on labor movement). The majority of projects have concentrated on infrastructure, where many projects in the pipeline existed and could be activated quickly, and where employment loss was concentrated, both domestically and in Israel (PCBS estimates that 38,000 construction jobs were lost between September and December 2000). Moreover, physical damage required repair and reconstruction.

¹²⁴ This compares with 1.2 million job-days which UNRWA planned to create in 2001 from US\$47 million allocated to job creation programs.

4.68 For all the positives, there are concerns about the emphasis of these programs on infrastructure. The first reason for concern is the high unit cost of a job-day – more than US\$50 on average. This should be compared with the US\$10-15 wage received by the worker, as well as with the implicit cost of maintaining a job in the PA (US\$23).¹²⁵ The reason for this, in turn, is that more than two-thirds of the project budget is commonly spent on construction materials and equipment.¹²⁶ A second related concern has to do with the Israeli origin of much of this construction material (especially tar and cement), which in turn depresses the multiplier effect of project civil works expenditures. A third concern is vulnerability to restrictions on the movement of construction materials within WBG and on their import from Israel, which has caused delays and added to costs. And a fourth is that construction programs do not target all groups, with skilled workers and women remaining largely untouched by them.¹²⁷ Above all, notwithstanding the psychological benefits for those who have received work, it must be concluded that these emergency employment programs have made no dent in WBG unemployment; 2 million job-days would represent full-time employment for only some 10,000 of the c. 264,000 currently unemployed – i.e. 3-4 percent of them.¹²⁸

4.69 The construction sector has not yet exhausted its potential for job creation, but other affected sectors such as tourism and agriculture also present significant rehabilitation opportunities, and more could be done on income generation activities successfully piloted on a small scale by NGOs. Expanding sector scope and project approaches would extend assistance to other socio-economic groups, and hence broaden and improve targeting. Above all, though, a way of scaling up the program at reasonable cost must be found if the objectives of the employment program as a whole are to be met. This issue is further discussed in **Chapter 5**.

4.70 Comparing employment schemes with cash/food distribution programs is not straightforward. The advantage of cash/food assistance is that a much larger proportion of the available funds end up directly in the pockets (and stomachs) of Palestinian households. In simple terms, about 90 percent of a cash assistance program should reach the beneficiaries, whereas the *most* labor intensive job creation programs can only expect 50-60 percent of the budget to accrue directly to the primary recipients.¹²⁹ The counter arguments in favor of job

¹²⁵ Put another way, the PA's 120,000 jobs cost about US\$684 million on an annualized basis, i.e. around US\$5,700 per job. The emergency employment schemes collectively expect to create c. 2 million labor days from around US\$105 million in disbursements by the end of December 2001. If a working year consists of 250 days, then one job-year costs about US\$13,100 through the employment generation program – i.e. 2.3 times more than through support to the PA budget.

¹²⁶ This in part reflects the fact that a number of projects that were already in the pipeline were re-packaged as "emergency projects", which brought down the average labor content of the overall program. It should be possible to achieve a labor content of at least 50 percent for construction projects designed with careful attention to this specific issue.

¹²⁷ It should be noted, though, that 80-90 percent of women did not work outside the household prior to the *intifada*.

¹²⁸ This assumes that 200 days of work constitutes full employment. The labor force is currently estimated at 745,000 (excluding East Jerusalem) and unemployment at 35.5 percent, using the relaxed definition of unemployment (para. 3.10), giving an unemployed labor force of 264,000 (World Bank staff estimates).

¹²⁹ Activities such as cleaning, painting and terracing can ensure higher transfer efficiencies, but experience in earlier job creation programs has shown that the effects of these jobs are very short-lived and have tended to result in negative public perceptions (see Samia Al Botmeh and Edward Sayre, *Employment Generation Schemes in the West Bank and Gaza Strip*, Palestine Economic Policy Research Institute (MAS), 1996).

creation are very strong, however. These schemes provide communities with tangible assets (such as roads, buildings, sidewalks, etc.) and can contribute to workers' skills. All-importantly, should the non-wage component be spent on *local* materials, the multiplier effect for the Palestinian economy can be comparable to what is achieved with cash assistance. Finally, job creation programs have the strong advantage of self-targeting and thereby reaching the truly needy, since they offer little to people already employed or with high reservation wages.¹³⁰ Dependency is also not created by such schemes, which are self-limiting.

4.71 **Reconstruction.** Some US\$45 million has been committed to the reconstruction of damaged buildings, houses and general infrastructure and the rehabilitation of damaged land, most of it from IDB (US\$22 million), and the rest by UNRWA and within existing job creation programs.

4.72 **Gaps in Emergency Provision.** A number of needy sectors have escaped much donor attention – in particular *the municipalities, regular service delivery* and the *private sector*. **Chapter 5** will propose approaches that can be adopted to help fill these gaps.

- *Municipal governments.* The municipalities have not received much systematic financial or technical assistance from the PA or the donors, and will need budgetary assistance if they are to continue to deliver basic municipal services under current conditions.
- *Regular service delivery.* The squeeze on operating costs has been described at some length in this chapter. Resolving this issue is of great importance, particularly if the quality of health and education services is to be preserved against further decay. The sums involved are relatively small, and targeting mechanisms are available.
- *The private sector.* Steps need to be taken to prevent viable firms that cannot get access to credit from folding. In addition, the groundwork for a private sector post-conflict facility should be laid now, so that assistance can be provided as soon as demand begins to recover. Action at the policy level also should not wait; the PA's goal should be to prepare as conducive a climate for investment as possible.

4.73 **Donor Coordination.** The *intifada* has challenged the mechanisms for capital-level and local donor coordination established after Oslo. These were uniquely tied to the peace process and took as their starting point, and as a key objective, trilateral cooperation among the donor community, the Palestinian Authority, and the Government of Israel. Two important evaluations of the structure were carried out for the AHLC in recent years, one by the World Bank in its role as AHLC Secretariat and the other by the World Bank and the Government of Japan. Their essential conclusion is that the structures, while complex, were generally rated as effective by all stake-holders, while the AHLC evaluation underscored that the system conformed to DAC principles and best practices. The emphasis of the two reports was on enhancing PA ownership, shifting the focus to the longer term (with the use of the Palestinian Development Plan and the Comprehensive Development Framework as tools in this endeavor) and on the quality and transparency of aid/resource management.

¹³⁰ The wage at which an individual will accept work.

Box 22: Evaluating the West Bank Gaza Aid Management Structures

The AHLC Secretariat report of September 1999 notes that “the existing aid coordination structure provides a strong platform to build on, and the PA and donors have a common interest in maintaining and strengthening it. At the same time, the aid management system needs to become less dominated by the donors and less biased to the short term. Both sides need to guard against tendencies that could undermine the quality of aid and resource management. On the donor side the danger is that short term efforts to deliver aid quickly and to reflect individual donors’ special interests can undermine Palestinian institutions and direct aid to activities that are unsustainable. On the PA side, the danger is that the resentment of perceived donor domination will compromise the quality of PA participation in joint bodies and prevent genuine dialogue. In line with the DAC principles for aid coordination, the starting point for aid coordination should be a strong planning and resource management framework (i.e. it should be process-oriented and address the roles of all relevant actors and all elements of the strategy)”.

The World Bank/GOJ Aid Effectiveness Study states that “the structures of aid coordination have evolved considerably since 1994, serving to enhance the effectiveness of donor assistance. But there is room for further improvement. Donor coordination mechanisms should be better integrated into the Palestinian development process with the PA assuming the lead role in donor coordination. The documentation and transparency of managing and coordinating aid needs to be strengthened with a bigger role for NGO involvement.”

Sources: “Improvement of Aid Coordination for West Bank and Gaza”, AHLC Secretariat, September 1999 (published June 2000), and “Aid Effectiveness in the West Bank and Gaza”, Government of Japan and the World Bank, June 2000.

4.74 With the coming of the *intifada*, the aid community suddenly faced a situation in which the longer term was no longer paramount, and in which the trilateral basis for cooperation that underlay the structures was, at best, suspended. In addition, the PA became overwhelmed with the political dimensions of the *intifada* and the need to manage each day as it came, and its ability to exercise leadership in the donor arena diminished – a process reinforced by reduced financial and operational resources, movement difficulties and the daily disruption of normal working life by the conflict. The entire aid community was also challenged by the roller-coaster nature of the crisis, which has been punctuated by periodic expectations that the full range of coordination mechanisms could be reactivated.

4.75 Donors adapted variously to this situation in which the official trilateral structures could not be relied upon. First, there was a substantial level of *informal coordination*. In the first months of the *intifada*, both major local coordination bodies, the all-inclusive LACC and the smaller JLC, met even without the presence of Israeli authorities. At the capitals level, an “informal” donors AHLC took place in Stockholm in April 2001, including active participation by the Islamic Development Bank, and representing the culmination of a concerted effort to mobilize budgetary support. Throughout the period, the donor members of the JLC have also consulted regularly on policy and operational issues. Some *formal coordination* has also been sustained. Here, donors concentrated on sectoral issues, including through an informal Humanitarian Task Force which acted as a forum for information-sharing and the coordination of emergency assistance among donors, UN agencies, NGOs and the PA. Those Sector Working Groups (SWGs) operating in the humanitarian arena have been active (e.g. Health, and Education), including an *ad hoc* SWG on Job Creation that was revived after having been phased out in 1997. Several other SWGs have continued to meet during the *intifada*, albeit with less frequency (e.g. Industry, and Water). Thanks largely to the diligence of the IMF and the commitment of key donors involved in budgetary support such as the EU, there has in effect also been a “rolling” SWG on Public Finance. In addition, the technical Task Force on Project

Implementation has remained open as a channel for donors to express collective concerns on project implementation to the Israeli authorities.¹³¹

4.76 Nonetheless, donors interviewed for the *Assessment* in late 2001 expressed a common view that information flows among the wider donor community have not been adequate, this being a particular frustration for smaller bilateral donors. More critical, efforts to broker a strategic exchange between donors and the PA, and within the broad donor community, have not been given sufficient attention. After one year of *intifada*, donors concluded, the LACC co-chairs needed to rectify this shortcoming. A series of meetings was held around this *Assessment*, including informal (donors only) LACC meetings in November 2001 and January 2002, and an informal (donors, PA) JLC meeting in November 2001. In addition, MOPIC and UNSCO have launched an initiative to revitalize the SWG structure. Several meetings of SWG shepherds have taken place in recent weeks, and agreement has been reached on designating a subset of “priority SWGs” that would focus their energies on fleshing out the programmatic recommendations of the *Assessment*¹³² and working with the PA on the preparation of a Palestinian Emergency Plan (**Chapter 5**). The SWG co-secretariats, UNSCO and the Bank, will provide database support to this effort as well as disseminate findings and experiences and help MOPIC establish the long-delayed donor website.

Boxes 23 – 28: Six Donor Responses to the Crisis

Box 23: USAID

The USAID Mission to the West Bank and Gaza has made significant program changes since the beginning of the *intifada*, in response to urgent needs and opportunities, and in light of what is practical in implementation terms. The current project mix combines “emergency response” activities with a continued focus on long-term development projects, including appropriate institutional development assistance.

“Emergency response” programs under implementation amount to US\$43 million in commitments, for short-term job creation, emergency health assistance (the delivery of emergency medical supplies and equipment, training for emergency personnel, and funding for psycho-social treatment), support to UNRWA, emergency micro-finance support programs, direct assistance to Palestinian NGOs providing services to vulnerable groups and employment creation programs, short-term training and business internships, and expanding the scope and geographic coverage of USAID’s small-scale community services. Due to the nature of USAID’s engagement, its assistance program is delivered by NGOs and the private sector.

Some “longer-term” development programs funded by USAID continue, including support for policy and institutional development. The focus on providing water infrastructure in both Gaza and the West Bank remains, with on-going well drilling and pipeline construction, and designs underway for a North-South Gaza water carrier, a Hebron wastewater treatment plant, a Gaza desalination plant, and the Southern West Bank village water network. The total anticipated cost of these 5 programs is c. US\$200 million. USAID-funded programs to strengthen the judicial system, develop the private sector environment (including new laws and institutional frameworks), promote investment, develop maternal-child health care, and the higher education system continue, albeit more slowly than before.

¹³¹ In calmer times, the Task Force also serves as a forum to address issues between donors and the PA.

¹³² These are the SWGs for Public Finance, the Private Sector, Education, Health, Water and Wastewater, Energy, Agriculture and Employment Generation. The need to coordinate efforts on food and cash assistance was also recognized, either through a sub-group of the Employment Generation SWG (since both activities aim principally to provide short-term income support), or by setting up an *ad hoc* SWG, as had earlier been proposed.

USAID has also suspended or canceled a number of projects because of the confrontation. These include a proposed highway in the northern West Bank and Gaza, border industrial zones in Tulkaram and Rafah, and the planned procurement of high-tech scanners for use at border crossings.

Source: Interview with USAID Staff.

Box 24: Canada

Between 1995-2000 Canada committed some US\$74 million, and disbursed US\$60 million.

Since the start of the *intifada*, Canada has contributed the following from various heads to the emergency:

- US\$3.5 million for employment generation. These funds are being administered by the World Bank through the PEACE Facility. Projects covers both West Bank and Gaza and are being implemented by the Ministry of Local Government.
- US\$2.1 million for various emergency activities, including UNRWA emergency appeals, a World Vision appeal, and health appeals by ICRC, UPMRC, UHWRC and the Friends of East Jerusalem Hospitals.
- US\$0.55 million for the psycho-social and physical rehabilitation of Palestinian children. The program has 7 Palestinian NGO partners in WBG, and is coordinated with the Secretariat of the National Plan of Action for Palestinian Children.

For fiscal 2001/2002, the planned Canadian contribution was c. US\$14 million. (\$20.3 million Canadian). In response to crisis, an additional US\$4.5 million was committed, bringing the total planned to 26.8 million Canadian (some US\$17.2 million) for the current fiscal year ending March 31, 2002.

Source: Interviews with Canadian Representative Office & MOPIC, October 2001.

Box 25: UNDP's Program of Assistance to the Palestinian People

UNDP/PAPP responds directly to needs identified by its Palestinian counterparts, including governmental institutions and civil society organizations, as well as to the priorities identified by donors. Priority is always given, when feasible, to projects with sustainable developmental impact and to UNDP's overarching corporate goal of poverty alleviation. Extensive consideration is given to local conditions and constraints, including restrictions on movement, the vulnerability of individuals, and the availability of material. PAPP concentrates on small-scale projects with high labor content and a minimum of dependence on imported materials. Implementation responsibilities and monitoring systems are totally decentralized to overcome closure restrictions. The projects implemented under the umbrella of the PAPP have been formulated in direct response to the Palestinian Emergency and Relief Plan produced by the Ministry of Planning and International Cooperation in January 2001.

Over a dozen separate projects have been launched in support of employment generation activities and emergency health, with a total budget of US\$27 million. To date, disbursements total US\$18 million, and 350,000 work-days have been generated in over 120 localities. Thousands of dunums of damaged land have been replanted, over 60 schools and kindergartens rehabilitated, over 50 private homes and public facilities restored, several localities provided with improved internal roads and water and sanitation systems, and 14 new health facilities developed and equipped.

Source: Interview with UNDP Staff.

Box 26: The European Union

The European Union¹³³ significantly stepped up its assistance and has committed over US\$400 million since the beginning of the *intifada*, while having disbursed over US\$300 million of this by the end of December 2001, US\$245 million of it in 2001 itself. EU disbursements represented 26 percent of the total for 2001, and more than a doubling of previous annual disbursements.

In addition, the EU provided some US\$215 million in 2001 to UNRWA for the agency's general fund, its emergency appeals and for food aid (US\$135 million from EU Member States and US\$80 million from the European Commission). The EU's main instrument to respond directly to the crisis has been the EU budget managed by the European Commission. The Commission has adopted specific emergency response initiatives in parallel to its regular development program, significantly increasing the funding made available for the West Bank and Gaza. When compared to previous years, commitments have risen from approx. 60 million Euros in 1999 to over 210 million Euros during the *intifada*.

Within the emergency category, some 48 million Euros were allocated through the EC Humanitarian Office (ECHO) since September 2000 -- in particular for direct food assistance and for post-injury rehabilitation, psycho-social support and non-food humanitarian items. This represents a four-fold increase compared to the period before the *intifada*. A further 29 million Euros were allocated for a food security programme to be implemented jointly with UNRWA, both for a) food assistance through UNRWA's Relief & Social Services, Health and Education Programmes; and b) cash assistance for special hardship cases. Budgetary support disbursements to the PA reached 128 million Euros by the end of December 2001, well exceeding the initial allocation of 25 million Euros.

In addition, regular EC-funded projects have continued to be implemented throughout the first year of *intifada*. Bilateral assistance disbursements to the PA and civil society amounted to 28 million Euros, particularly for infrastructure development, capacity building, job-creation, social assistance and institutional reform. Furthermore, rapid disbursements in February and March 2001 of 15 million Euros to the Municipal Support Programme and the Local Rural Development Programme for labor-intensive construction projects have ensured the provision of 200,000 labor days for unemployed Palestinian workers.

Source: EC Technical Assistance Office, West Bank and Gaza.

Box 27: Japan

Japan has supported the Palestinians with a total amount of US\$619 million since 1993.

Japan's assistance focus on "3 Building Blocks":

- Human resource building
- Legal/institutional building
- Physical infrastructure building

Japan's assistance priority areas:

- Basic human needs, such as education, environment, health and water resource
- Emergency employment generation
- Small-scale projects for rural communities
- Japan-PA-Israel trilateral projects
- Assistance to Palestinian refugees

Since the outbreak of the current *intifada*, Japan has contributed US\$46 million, as follows.

Direct Assistance to the Palestinian Authority

- US\$2.63 million for Expansion of Immunization Program
- US\$2.24 million for Food Aid Program
- US\$3.26 million for Increase of Food Production Program

¹³³ Including bilateral EU Member States support and multilateral European Commission support.

Small-Scale Projects for local communities

US\$3 million for 42 projects

Through UNDP-PAP

US\$7.85 million for General Support for 2001

US\$4.04 million for Emergency Job Creation US\$0.50 million for Emergency Health Aid

Through UNRWA

US\$13.23 million for Food Aid Program for 2000 and 2001

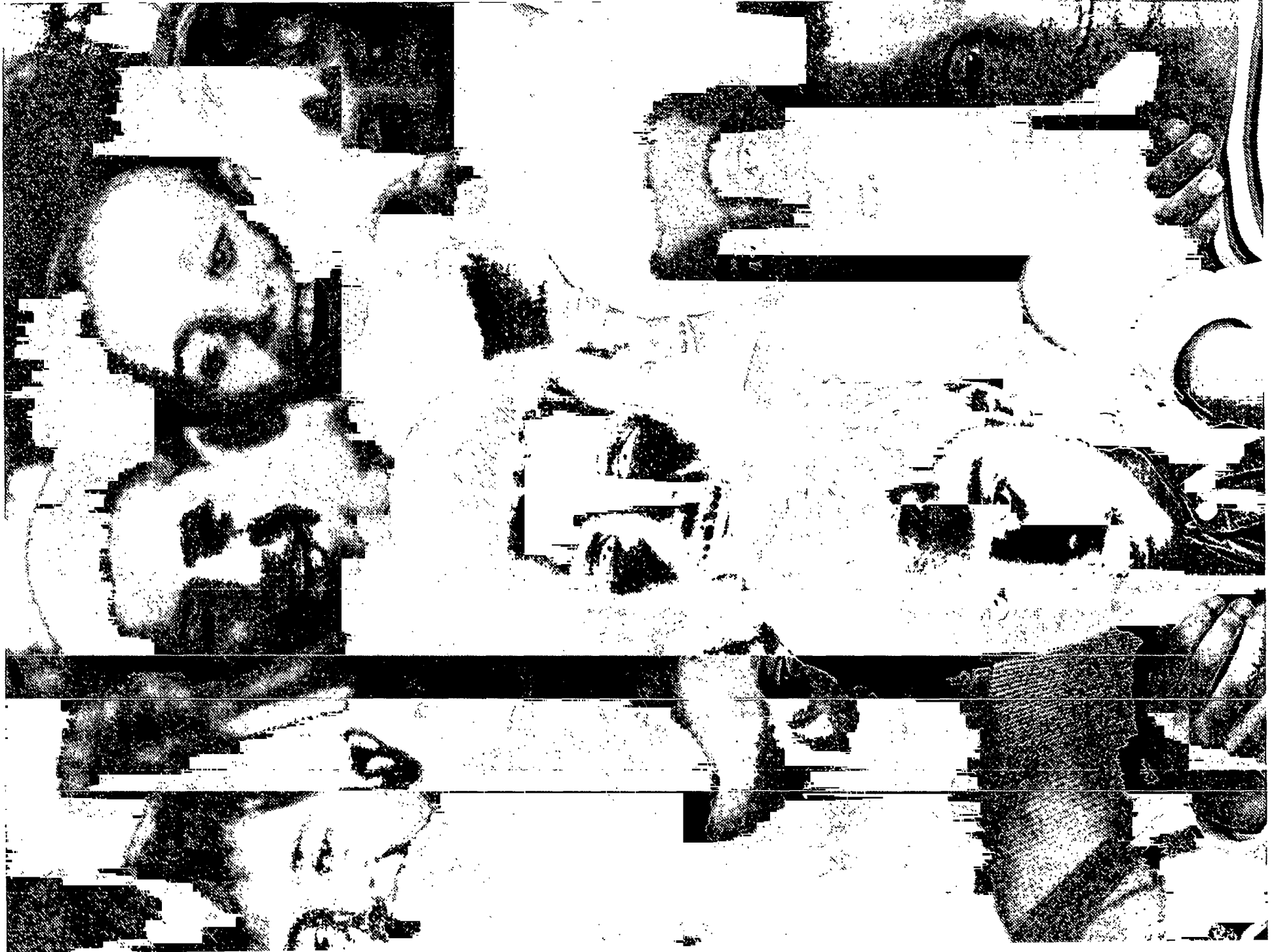
US\$9.22 million for General Support for 2001

The Japanese government assistance during this difficult period has been made not only in response to the emergency needs, but also in consideration of development needs with a mid to long term point of view.

Source: Embassy of Japan, January 2002.

Box 28: Norway

The Norwegian Representative Office to The Palestinian Authority has during 2001 and 2002 continued to implement its main programs of long term development assistance. The programs in infrastructure and institutional development have been adjusted to the ongoing crises within the allocated budget. In 2001 the total Norwegian contribution was US\$43 million. This included support to UNRWA of US\$11 million, budget support US\$10 million and labor intensive projects of US\$7.9 million. The labor intensive projects were a response to increased unemployment and poverty. They created 350,000 workdays and were implemented in different local communities through the municipalities, in close co-operation with relevant ministries. All grants were channeled through the Ministry of Finance. Labor intensive projects will continue in 2002, with an increased focus on the private sector in the local communities.



5. A WAY FORWARD

THE ECONOMIC OUTLOOK FOR 2002-3

Three Scenarios

5.1 Three illustrative scenarios have been developed by the World Bank, and these clearly show the impact of political developments on the economic prospects for the West Bank and Gaza.

- The first scenario assumes a continuation of the *status quo* pertaining for much of the *intifada* – i.e. an equivalent level of closure and confrontations with restricted movement of goods and people still possible, continued access by 50,000 laborers to Israel, donor budget support maintained at projected levels (c. US\$64 million per month), and no payment of tax revenues due the PA by Israel.
- The second scenario assumes that there is an early *political rapprochement* -- leading to a cessation of hostilities, a lifting of closure and a resumption of revenue transfers by Israel.
- The third scenario assumes *harsher closure*, with armed confrontation resulting in considerable additional physical damage and heavy disruption of trade and movement, along with a virtual closing off of any labor access to Israel and the settlements. Donor budget support would continue at projected levels and there would be no payment of tax revenues due the PA by Israel.

5.2 Several conclusions arise from this exercise. *First*, a continuation of current circumstances would further erode the living standards of the population, albeit at a slower pace than during the last year. *Second*, a lifting of closure would have an immediate and significant economic impact. *Third*, even if closure is lifted and relations normalize, per capita income will take *at least* two years to return to pre-*intifada* levels, and will only do if private sector confidence in the future of the economy can be significantly restored; it would take much longer than two years to restore the real per capita income levels prevailing in 1994. And *fourth*, a further radical tightening of closure, with or without the demise of the PA, would push the Palestinian economy in a poverty trap in which any prospect of recovery can be forgotten for a long time.

Table 23: Three Economic Scenarios for the West Bank and Gaza, 2002-2003

<i>Macro-economic Trends Under Different Scenarios</i>	<i>Status Quo</i>		<i>Lifting of Closure</i>		<i>Harsher Closure</i>		
	2001	2002	2003	2002	2003	2002	2003
Gross National Income (GNI), US\$ million, current prices	4,609	4,656	4,746	5,620	6,716	3,834	3,794
Gross Domestic Product (GDP), US\$ million, current prices	4,093	4,129	4,209	4,853	5,714	3,713	3,671
<i>Real annual change:</i>							
GNI per capita	-19%	-3%	-3%	17%	14%	-20%	-5%
GDP per capita	-16%	-4%	-3%	13%	13%	-13%	-5%
Private Consumption	-14%	0%	4%	16%	19%	-19%	0%
Total Fixed Investment	-30%	-6%	-3%	31%	27%	-36%	-5%
Export	-8%	-4%	15%	13%	35%	-3%	-4%
Import	-19%	-5%	4%	12%	22%	-28%	-1%
Unemployment rate	26%	28%	29%	21%	15%	36%	37%
Poverty, share of population below poverty line	46%	50%	51%	39%	29%	62%	65%

Note: All data excludes East Jerusalem

Source: World Bank Estimates.

The Status Quo Scenario

5.3 The *Status Quo* scenario would result in a relatively stable level of economic activity with a small positive growth in GDP and GNP. It would not, however, be sufficient to maintain per capita income levels. Poverty would stabilize at around 50 percent of the population, with absolute numbers increasing. Investment would further decline in favor of immediate consumption. The strong downward pressure on wages induced by high unemployment levels would permit Palestinian exporters to regain some of the market share they have lost from disruption of their activities.

5.4 This scenario assumes that PA spending is held to a monthly average of US\$90 million in current expenditures, plus US\$1 million in capital expenditures. Monthly revenues would continue their slow decline, to only US\$15 million per month. Currently, potential donor recurrent cost commitments appear likely to materialize at c. US\$64 million per month in direct support, with at least another US\$3 million per month in support for non-salary operating costs under the *Emergency Services Support Program* (para. 5.18) – a total of some US\$804 million for the year. Consistent with the fiscal framework established for 2002 with the IMF, closing the central government fiscal gap of US\$76 million per month would require donor contributions of US\$912 million for the year under this scenario; this would permit the PA to avoid running up additional arrears, which have reached unsustainable levels (currently estimated at US\$430 million at year's end, para. 3.35).

5.5 Were Israel to transfer the stock of arrears owed to the PA (estimated at NIS 2.1 billion – or approximately US\$0.5 billion gross at year's end, para. 0), this would permit the stabilization of the PA's arrears position and would enable a major injection of liquidity into the Palestinian

private sector. A resumption of regular tax clearances would bring an additional average of c. US\$29 million per month, enormously easing the PA’s fiscal position.

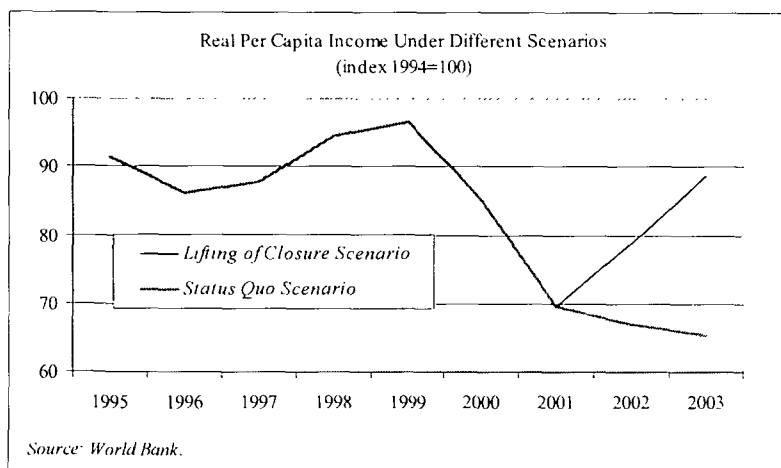
The Lifting of Closure / Optimistic Scenario

5.6 The keys to achieving a healthy recovery of the Palestinian economy under a scenario of political *rapprochement* lie in a removal of internal and external closures and the re-issuance of work permits in Israel to Palestinian workers. Lifting the closure would considerably lower the costs of doing business in WBG and would help stimulate a recovery of Palestinian private enterprise, while re-admitting workers would provide immediate relief to the unemployed, raise average incomes and worker productivity and provide an important injection of cash into the Palestinian economy. It is assumed that the monies owed to the PA by Israel would be released under a scenario of *rapprochement*, and that regular monthly transfers would resume.

5.7 After two years, the formal unemployment rate (para. 3.10) would likely decline from 26 percent now to about 15 percent in end-2003, compared with 10 percent prior to the *intifada*. Even two solid years of economic recovery would not suffice to bring living standards back to their pre-*intifada* levels, and about 30 percent of the population would still be poor by the end of 2003.

5.8 Assuming unchanged tax policy, two years of economic recovery in 2002 and 2003 could return potential PA tax revenue to its 1999 level. The net fiscal position of the PA is more difficult to predict, as it will depend critically on the pace of expenditure and on the net stock of debt and arrears accumulated (arrears and loans, versus grants and withheld tax revenues), and the pace of its repayment. Even assuming a resumption of regular Israeli clearance transfers, tax revenue in 2002 would not be enough to cover a disciplined monthly expenditure level of \$91 million per month. To bridge the monthly fiscal deficit, c. US\$30-35 million would be required per month from donors (depending on revenue assumptions), for a total of c. US\$360–420 million for 2002. These transfers could then be tapered off in 2003.

Figure 15: Real Per Capita Income



The Tightened Closure / Pessimistic Scenario

5.9 This is not a sustainable economic scenario in any conventional sense, and would lead in all probability to a gradual fragmentation and dissolution of normal civil governance, capital flight and a reversion from modern business activity into barter trade and subsistence farming. Donor fiduciary standards would become harder to maintain. Dependence on food aid would

grow, as under such conditions a monetized economy has decreasing relevance for many (thus dampening the impact of many conventional donor contributions). Unemployment could climb to over 40 percent by the end of 2002, poverty rates could reach 60 percent of the population, and GNI per capita could fall a further 30 percent, to only half the pre-*intifada* level. Considerable physical damage and a dramatic drop in investment would significantly reduce the stock of productive assets, and in turn the ability of the Palestinian economy to recover when the crisis eventually ends. For emergency programming purposes, domestic revenue is assumed to decline to an average over the year of only US\$10 million, requiring US\$972 million in donor budget support to sustain a recurrent and capital spending level of US\$91 million per month.

The “Fourth Scenario”/PA Collapse

5.10 While this scenario has too many speculative elements to be worth formally modelling, it is not beyond the realms of possibility that the PA might cease to govern. Should this occur, the donors would lose their main conduit for support – the budget channel through the Ministry of Finance. The consequences of a simultaneous collapse of the administration, incomes and demand would set the peace process back many years and would undo almost all of the post-Oslo economic and institutional gains. While donors would presumably switch their efforts into emergency support, humanitarian relief and small-scale infrastructure delivered through a mix of UNRWA, NGOs and local governments, it would not be possible to transfer the same sums as under the first three scenarios.

Box 29: The World Bank’s Macro-Economic Model for West Bank and Gaza

In order to project macro-economic developments in the West Bank and Gaza, the World Bank uses a quantitative economic model which describes the economic relations between households, producers, government and the rest of the world through a set of accounting and behavioral equations. Both demand (intermediate consumption, final consumption, investment, government expenditure, exports) and supply (domestic production, imports) are modeled, with flexible prices clearing all markets (factor and product). Certain exogenous assumptions are made (to account for government expenditure, tax policies, foreign aid flows, population growth, factor productivity, worker remittances, and the prices of exports and imports) in order to simulate different outcomes. Thus the macro-economic impact of closure is captured through the following assumptions: a decline in worker remittances, in line with the observed decline; an increase in the price of imports, to reflect additional transaction costs; and a decrease in factor productivity, to illustrate the impact of internal closures on private business activities. The model captures the specificities of the Palestinian economy. Its parameters are calibrated using a large statistical database (a social accounting matrix for 1998) which depicts the behaviors of Palestinian economic agents. In its present form the model includes seven sectors of activity (agriculture, manufacturing, construction, transport and communications, commerce, other private services, public services) but can easily be disaggregated into 30 sectors of activity, and two different trade partners, Israel and the Rest of the World. The model reflects the current trade and fiscal arrangements with Israel. The model is also used to predict the impact of macro-economic development on poverty rates, and reflects the fact that in periods of depressed income, households reduce their savings and consumption of non-essential goods. The observed distribution of consumption in 1996-98 is in turn used to predict a national poverty rate for a given average per capita level of consumption.

Some Basic Assumptions Underlying an Economic Recovery

5.11 The scenarios described above are determined principally by political developments. It is clear from the experience of the 16 months of the *intifada* that determined management of the economy by the PA and a massive financial commitment by the donor community have failed to prevent economic crisis, though they have staved off economic disaster. It is clear from this

report that the proximate cause of Palestinian economic crisis is closure, and that lifting the closure is essential if the economy is to recover.

5.12 As described in detail in **Chapter 2**, the closure impacts in a variety of ways: domestic trade and service delivery are impeded by the system of checkpoints and blockades established throughout the West Bank and Gaza; trade with Israel and the rest of the world has become costly and unpredictable as a result of security checks and delays on the passage of goods and people from and into WBG; and the loss of work permits in the Israeli labor market has increased unemployment and reduced internal Palestinian demand. It follows that dismantling the system of internal checkpoints, easing of the restrictions at the borders and a reopening of the Israeli labor market to Palestinians will do more to stimulate economic recovery than any of the measures proposed to the donors and by the Palestinian Authority later in this chapter.

5.13 In addition to closure, two other important issues require resolution. The first is Israel's withholding of tax clearance revenues, monthly flows of which are estimated at US\$29 million per month under current economic conditions, with an accumulated stock of NIS 2.1 billion – or approximately US\$0.5 billion in gross terms as of the end of December 2001 (para. 0). Renewing monthly transfers would provide immediate fiscal relief and would permit donors to switch a portion of proposed budget support into productive, growth-oriented activities. Even more important, transferring the accumulated stock would enable the PA to clear the US\$450 million of PA and municipal arrears, the bulk of which is owed to the domestic private sector. These arrears have contributed to a major liquidity crisis in the Palestinian private sector, which is in turn threatening the solvency of the banking system, as described in para. 3.45 and **Annex 7**.

5.14 Mention must also be made of increasing military destruction of donor-funded projects, and the deterrent effect that such measures are having on commitments to the medium-term infrastructure program. Whatever the reasons may have been, destroying the runway at the Gaza Airport has been interpreted by many in the international community as a signal that internationally-financed developmental assets with no apparent security connection will not be exempted from the conflict. It is very important that the Government of Israel reverse this perception.

5.15 In a related vein, it will also be important that the activities of the Task Force on Project Implementation continue along the reinvigorated track proposed by the Government of Israel in recent contacts with the donor community. The TFPI was established prior to the *intifada* to serve as a forum in which donors and the Government of Israel would seek ways to resolve bottlenecks to donor project implementation. If the recent positive indications are followed by mitigating action on the ground, this would also help encourage a more vigorous donor re-engagement in major infrastructure activities with lengthy implementation spans.

RECOMMENDED DONOR ACTIONS

Emergency Support

5.16 Sustained donor commitment over the coming year is required under any of the scenarios described above. Priority emergency assistance needs for 2002 can be grouped into seven program areas (see Table 24 below). It is recommended that donors focus emergency support on these priority areas in 2002, while supporting improvements in the coordination process.

1. Budget Support

5.17 Additional budget support is vital to sustaining demand and preserving a minimum level of service provision. Under the *Status Quo scenario*, the central PA budget deficit net of tax revenue clearances is likely to amount to about US\$76 million per month, or US\$912 million for the whole of 2002. Under a *Lifting of Closure scenario*, Israel would resume the transfer of tax revenues, and this in combination with some recovery of domestic revenue would reduce the monthly budget deficit to an average of perhaps US\$30-35 million, requiring a more modest US\$360-390 million in donor support for the year as a whole. Under a *Tightened Closure scenario*, further revenue contraction would occur, and additional donor budget support totaling perhaps US\$972 million for the year would be needed to sustain a monthly recurrent and capital expenditure level of US\$91 million. The prospects for donor budget financing for 2002 are currently quite good. The Arab League states are considering a monthly contribution of US\$55 million, and the EU is likely to continue support at the same level as in 2001 (10 million Euros per month).

2. Support for Basic Service Delivery

5.18 There is a need to provide targeted operating cost support for the basic social services delivered by the line ministries and the municipalities, and supported by NGOs. Under the leadership of the Ministry of Finance, an *Emergency Services Support Program (ESSP)* has been prepared to cover unmet PA and municipal needs for the first six months of 2002; these needs total US\$85 million (US\$46 million for the PA and US\$39 million for the municipalities (**Annex 6**).¹³⁴ A further US\$71 million (PA US\$50 million, municipalities US\$21 million) would likely be required through a second ESSP to cover needs in the second half of the year, giving an overall total of US\$156 million under the *Status Quo scenario* (requirements would vary under the other two scenarios, see Table 24). To date, US\$58 million has been pledged by nine donors.¹³⁵ Most of the funds under ESSP would be disbursed against contracts for the purchase of drugs, food, fuel, rents, textbooks, spare parts, etc. PA ministry operating cost deficits specific to basic service delivery total about US\$8 million per month at present (in the Ministries of Health, Education, Social Affairs and Agriculture). In the case of the municipalities, unmet budgetary needs appear to average some US\$3-4 million per month.¹³⁶

3. Private Sector Support

5.19 The Assessment shows clearly that the private sector has been hard hit, has received relatively little donor assistance and is vital to any Palestinian economic recovery. Steps should therefore be taken to assist businesses weather the crisis, as well as to encourage investment once a political *rapprochement* is in prospect and demand begins to recover.

¹³⁴ The total proposed cost of ESSP 1 (January-June 2002) is US\$107 million, of which US\$21 million would go to the Labor Union's "Solidarity Fund" (cash unemployment benefit) and US\$1 million to emergency capacity building activities.

¹³⁵ Apart from the World Bank's US\$20 million, a further 43 million Euros has been pledged by the European Commission (20 million Euros) and up to seven member states.

¹³⁶ See paras. 0-3.34. Although municipal budget deficits appeared to total some US\$13-14 million for 2001 (c. US\$1 million per month), if allowance is made for forced budget reductions, unmet normal budgetary revenues totaled about US\$40 million (US\$3-4 million per month). The proposed allocation of US\$60 million to the municipalities under ESSP 1 and 2 allows for some limited labor-intensive service expansion.

- *VAT payments to suppliers.* Due to the fiscal crisis the PA has not been able to process VAT refunds to suppliers. This could be addressed through a concessional loan to the PA. The amounts owed are currently estimated at about US\$35 million. This loan would not be needed under a *Lifting of Closure scenario*.

- *A Private Sector Crisis Fund.* In discussion with other donors, the International Finance Corporation is designing a fund that would provide some support to businesses during the crisis, as well as finance a recovery phase once market demand revives (**Annex 7**). The Fund would not aim to compensate the private sector for the losses it has sustained; the objective, rather, is to provide financial and technical assistance to enable those enterprises able to function, even in a limited way, to weather the crisis, and to then assist businesses to restart operations quickly once the operating climate has improved. At present there are many businesses which remain viable but need advice on how best to manage the crisis. They also need access to capital to diversify activities and exploit some new export opportunities. Other businesses have lost buildings, inventory and equipment in the fighting, and need reconstruction assistance. Many others, however, cannot easily be helped until there is a resurgence of demand. Businesses that would qualify for assistance under the Fund would be those which have sustained physical damage or have suffered substantial economic injury as a result of the crisis, and are unable to obtain financial or technical assistance from other sources. Since most larger Palestinian businesses are able to seek financial support independently, the facility would thus target the small and medium enterprises that make up 90 or more percent of businesses in WBG (para. 3.41). It could also assist commercial banks to restructure their balance sheets once the crisis abates, by purchasing non-performing loans or providing tier-2 capital in the form of subordinated loans. The Fund could be managed by IFC using seconded experts, and would likely feature a number of windows, some of which would be activated during the crisis, others later. USAID, through its *Palestinian Enterprise Revitalization Program*, could complement the activities of the Fund with business development services and financial facilitation assistance.¹³⁷ Before developing the Fund in detail IFC and the World Bank will explore with donors their potential interest in contributing grants or soft loans to the facility. Under a *Status Quo scenario*, a sum of US\$40 million would be sought to provide support in the current phase, and another US\$100 to finance a recovery (under a *Lifting of Closure scenario*).

5.20 Thus far no funds have been subscribed to the activities proposed above.

4. Support for Employment and Welfare Schemes

5.21 The past year has witnessed substantial activity designed to offset the loss of employment in Israel and WBG, with a large number of different schemes providing jobs, cash and food through multiple distribution channels ranging from UNRWA, MOSA and the municipalities to

¹³⁷ Possibilities include support for initiatives such as Palestinian Banking Corporation's (PBC) program to restructure the financing of failing enterprises, especially tourism projects, and to convert dormant tourism infrastructure assets to alternative uses (e.g. the use of hotel as office space). Also of interest are recent efforts by the Small Business Administration in the USA to support post-September 11 business failures by providing grants for fixed costs to businesses to enable them to survive a period of low demand. In addition, there is a need to build local capacity to address the wave of insolvency while simultaneously improving the legal framework dealing with bankruptcy (such that appropriate forms of company organization and restructuring are legally sanctioned).

a wide variety of NGOs. The use of food aid in WBG is somewhat controversial (para. 4.64), and it would be worth considering the development of a food stamp program as an alternative to the distribution of food commodities.¹³⁸ In the event of a *Tightened Closure* scenario, though, the need for food aid will increase, and more food is likely to be made available through UNRWA and the World Food Program. Under the *Status Quo* and *Lifting of Closure* scenarios the main need will be for income support and employment creation schemes.

5.22 The extent of *cash* payments to the unemployed and the poor is not well-known and the administration of the various programs suffers problems ranging from lack of funds to suspicions about targeting (para. 4.64). There is a plausible case for such payments, not only for “hardship cases” (and/or the unemployable), but also to those who have lost their jobs -- because emergency job creation schemes have not so far made any serious impact on unemployment (paras. 4.68-4.69). *Job creation* schemes have been generally well-implemented and have advantages which include the building of assets and self-targeting. Improvements can be made to the design of current programs in order to a) emphasize the use of local materials (increasing the multiplier effects in the domestic economy); b) raise program labor content and broaden programs out beyond infrastructure to give greater emphasis to income-generation activities; and c) support employment in the private sector.¹³⁹ Above all, however, ways of scaling up job creation programs need to be explored. In other parts of the world the constraints to scale have been addressed by switching from a supply-led, engineering intensive approach to one in which block grants are provided to communities, and in which the control of procurement and project management is devolved to local governments. The scope for such a program in WBG should be explored without delay.

5.23 NGOs are heavily involved in the provision of cash support and increasingly in job creation (para. 4.50), and there is scope for increasing their role in these areas. At the same time, over 50 “Islamic” NGOs have been closed down by the PA on account of their allegedly extremist tendencies. Some of these NGOs are well-financed,¹⁴⁰ and offer emergency support as well as non-emergency social services (in particular pre-school and health programs). It is very important that the populations served by these NGOs, who live in some of the poorest areas in WBG, do not find themselves without basic support services.

5.24 Several recent proposals have been made to address the needs of the unemployed, the poor and the potentially unserved, through the creation of variously-structured funds. One proposal calls for the establishment of a fund to provide regular cash payments to some 110,000 unemployed workers, using international management expertise to ensure fair and transparent administration. This fund is sized at c. US\$400 million over two years. Another proposal calls for the establishment in PECDAR of a humane assistance department to provide support for the

¹³⁸ Food stamps, which could be converted to food at local shops, would have two advantages: first, they would remove some of the stigma associated with lining up for food at distribution centers; second, they would provide more support the local economy.

¹³⁹ For example, in the Gaza industrial estate, the PA has offered factory-owners 50 percent of the wage of any additional employee hired for a defined period of time.

¹⁴⁰ According to the Ministry of NGO Affairs, 54 out of more than 100 such organizations were closed by the end of January 2002. If one assumes that c. US\$100 million per annum was being directed to “Islamic” NGOs from private external sources before the *intifada*, the sudden loss in resources as a result of the banning of these NGOs could amount to at least a half of this amount. Nor is it apparent that these funds would be available to secular NGOs.

unemployed and the very poor through NGOs, local governments and MOSA (via grants to the poor and homeless, labor intensive micro-projects, salary cost-sharing with public and private employers). A third calls for the establishment, under MONGOA leadership, of a consultative board of PA, NGO and civil society representatives to identify emergency and poverty alleviation needs and channel money through civil society organizations to address them.¹⁴¹ Required funding in this case is estimated at some US\$200 million over three years.

5.25 It is important that any new initiative take its place alongside other emergency priorities, consistent with the joint PA-donor vision emerging from the *Assessment* process. If this is not done, these initiatives will overlap other efforts and will either divert funds needed elsewhere or, more likely, will fail to receive much donor support. That said, the limitations of current employment and welfare schemes are clear, and new thinking is called for. Employment programs are popular among donors, but need scaling up; donor support for cash payments has been lukewarm. A variety of approaches are possible – ranging from the intensification of existing programs to the creation of a new funding instrument. Accordingly, donors and the PA should, over the coming weeks, carry out a joint programming exercise. This exercise is needed both to crystallize the lessons learned so far from job creation and cash transfer schemes, and to take account of the emerging gaps in NGO emergency and basic service provision.

5.26 It is estimated that some US\$80 million has been committed already to welfare and employment schemes for 2002. At least US\$200 million could be absorbed if a concerted effort were made to develop more effective instruments; under a *Lifting of Closure* scenario the need for such support would diminish somewhat, while its importance would clearly rise under a scenario of *Tightened Closure*.

5. Physical Reconstruction

5.27 The *Assessment* estimates damage to infrastructure and land as of December 31, 2001 at US\$305 million. Only some US\$50 million has been allocated by donors as direct rehabilitation grants, mostly by IDB. A large portion of the damaged agricultural land cannot be rehabilitated due to its proximity to borders or flashpoints, and repair of some of the urban damage should await more peaceful times; for this reason, and in consideration of the fact that employment schemes would cater to some of the damage, a further US\$75 million might be sought from donors for a total of US\$125 million for reconstruction work in 2002 under a *Status Quo* scenario. Should there be a *Lifting of Closure* and a political *rapprochement*, the sums sought could increase; under *Tightened Closure* it would probably not be possible to do more than under *Status Quo*, due to restrictions on the movement of people and goods. Physical reconstruction work also has the added benefit of creating work; assuming an average labor content of 30 percent, US\$75 million could create some 1.5 million job days.

5.28 Particular mention should be given to the need for funds to repair and rebuild private housing. Over 500 housing units in the West Bank and Gaza have been destroyed,¹⁴² and up to

¹⁴¹ MONGOA's proposal calls for the board to represent the 6 "secular" NGO networks, which between them account for some 600 of the 900-plus NGOs in WBG. This initiative responds specifically to the closure of "Islamic" NGOs and is being developed in coordination with several PA agencies, for example MOPIC, the Ministry of Social Affairs and PEC DAR.

¹⁴² According to the Ministry of Housing, some 720 houses had been severely damaged or destroyed by the end of January 2002.

14,000 damaged in some manner,¹⁴³ at an estimated cost of US\$32 million. The PA has determined that owners whose houses were destroyed in the conflict should be given new purpose-built houses; standard designs have been developed and the houses could be built through UNRWA or under the World Bank's *Palestinian Housing Project*. More generally, the various reconstruction needs could be packaged for donor financing purposes either on an area-specific basis¹⁴⁴ or as sectoral projects (in roads, social infrastructure, etc.).

6. Student Scholarships

5.29 These could be provided to pupils and students unable to pay school/university fees, as a way of supporting their continuation in study and sustaining the financial viability of institutions of learning. A notional allocation of US\$20 million is proposed under the *Status Quo scenario*, to help mitigate the damage caused to the future human capital stock from long periods of enforced absence from study, particularly at the university level. As mentioned in para. 4.34, the Student Revolving Loan Fund offers one channel for such assistance.

7. Support for UNRWA

5.30 UNRWA will require additional funding for its emergency appeals. The Third Emergency Appeal is still short by US\$14 million, while the Fourth Emergency Appeal for 2002, requesting US\$117.6 million, was launched in December 2001 and is as yet unfunded. Donors should aim to fund the unfinanced balances of all of UNRWA's appeals since October 2000, which total some US\$142 million.

Total Financing Requirements for 2002

5.31 Table 24 estimates the cost of financing the seven priority programs, and the funds that appear to be available for them at this stage; it should be understood that both sets of figures are indicative. What the table shows is that somewhere between US\$1.1 billion and \$1.7 billion is needed, and that of this some US\$956 is likely already available. Whereas the needs are essentially covered if there is a *Lifting of Closure*, the same is not true under either the *Status Quo scenario* (an additional US\$578 million required) or under *Tightened Closure* (US\$766 million more needed). Further prioritization is therefore called for, and this is addressed in the paragraphs below.

¹⁴³ Source: Ministry of Public Works.

¹⁴⁴ Thus packages could be designed for North Gaza, Gaza City, Khan Younis and Rafah; and Ramallah/Al Bireh, Hebron, Bethlehem, Jenin and Tulkarem.

Table 24: Emergency Donor Support to the PA for 2002 under Three Illustrative Scenarios (US\$ million)

Scenario Program	Status Quo			Lifting of Closure (Optimistic)			Tightened Closure (Pessimistic)		
	Need	Available	Gap	Need	Available	Gap	Need	Available	Gap
1. Budget Support	816	768	48	300-360	768	--	876	768	108
2. Service Delivery (PA)	96	36	60	60	36	--	96	36	60
<i>Sub-total PA budget support</i>	<i>912</i>	<i>804</i>	<i>108</i>	<i>360-420</i>	<i>804</i>	<i>--</i>	<i>972</i>	<i>804</i>	<i>168</i>
Service Delivery (Municipal budget support)	60	22	38	40	22	18	70	22	48
3. Private Sector Support (Crisis Fund, VAT)	75	--	75	140	--	140	75	--	75
4. Unemployment and Welfare	200	80	120	150	80	70	250	80	170
5. Physical reconstruction	125	50	75	200	50	150	125	50	75
6. Student Scholarships	20	--	20	20	--	20	30	--	30
7. UNRWA	142	--	142	142	--	142	200	--	200
<i>Totals</i>	<i>1534</i>	<i>956</i>	<i>578</i>	<i>1052-1112</i>	<i>956</i>	<i>96-156 540**</i>	<i>1722</i>	<i>956</i>	<i>766</i>

** Were all PA central budget commitments fungible, the gap would range between US\$96-156 million. If none of the PA central budget commitments could be switched into investments, the gap would become US\$540 million (unfunded programs # 2-7).

Reviving Coordination Among Donors, and Between Donors and the PA

5.32 **Helping Develop a Palestinian Emergency Plan for 2002.** The donors should support efforts by the PA to develop the Plan (see paras. 5.39 and 5.49 below).

5.33 **Supporting the Strengthening of the Core Economic Management Institutions of the PA.** Donors should also make a concerted effort to support the further institutional development of MOPIC, MOF and MOET (see paras. 5.39 and 5.49 below).

5.34 **Reanimating Local Aid Coordination.** The apex coordination structures, in particular the Local Aid Coordination Committee (LACC), need to meet regularly to exchange information, share experiences and discuss common strategies. If this is not possible in the full tri-partite format, donors should seek to meet regularly with the PA and also among themselves. Donors also need to provide data on commitments and disbursements to MOPIC regularly.

5.35 The Sector Working Group (SWG) structure offers a viable means for further developing priority emergency programs for 2002, and appropriate SWGs should be directed to focus on the preparation of the proposed Palestinian Emergency Plan.¹⁴⁵ Thematic areas of focus include budget support (including the adequate provision of operating costs); basic service delivery (in particular the services delivered by the Ministries of Health and Education and the municipalities); emergency assistance to the private sector; additional support for social welfare and employment creation schemes (in particular the services delivered by the Ministry of Social Affairs and UNRWA); and the reconstruction of damaged infrastructure/rehabilitation of degraded land.

Box 30: Joint Programming and Harmonization

Over 60 bilateral and multilateral donors are involved at various levels in providing assistance to the Palestinian people, making aid coordination in WBG an enormous challenge. While assistance has by and large been well coordinated, difficulties have inevitably arisen. Donors have different policies, procedures and priorities, making it difficult for the Palestinian Authority to manage assistance at the aggregate level.

In an AHLC Secretariat report written in September 1999 (Improvement of Aid Coordination for the West Bank and Gaza), recommendations on improving aid coordination included *greater harmonization of donor programs and joint programming*.

Over the following year, donors worked together with the PA to improve aid coordination in various ways:

The Japanese Government financed the creation of a World Bank-UNSCO-managed website (International Assistance to the Palestinian People) in order to provide provides a common, widely accessible platform for the dissemination of development information;

In 1999, the Comprehensive Development framework was launched and a first phase, involving the preparation of 13 sector matrices, was developed. Successful transfer of the management of the CDF process to MOPIC was accomplished the following year.

Only during the *intifada* did donors really start to explore ways of better harmonizing their assistance. The crisis prompted the revival of the Emergency Employment Sector Working Group, led by Sweden, in which donors, PA agencies and NGO participants worked together in several emergency task forces at to assess needs and solicit community input to prepare a \$200 million program of emergency employment under enormous time constraints. The *Assessment* has proposed that the PA and donors should now work together on jointly programming a

¹⁴⁵ See also para. 4.76.

Palestinian National Emergency Program for 2002. Progress on harmonizing planning has also been made in the education and health sectors through the SWG structure; both sectors feature strong PA leadership.

The donor community should build on these experiences and move towards greater harmonization of procedures, both in order to support mainstream PA processes as well as to minimize the work associated with administering multiple donor programs. Initial steps can consist of uniform procedures for channeling funds and administering project accounts, the adoption of common procurement and auditing methods and the eventual provision of pooled budget support to sector programs on the basis of an agreed set of policies and investments, and reliable systems of program supervision and financial control.

Recommitment to the Medium-Term Development Agenda

5.36 Disbursements for infrastructure and technical assistance programs with a medium-term focus fell significantly during the *intifada* (from US\$482 million in 1999 to US\$175 million in 2001). There is a need for donors to do all they can to sustain these developmental activities, since they embody higher economic returns than most emergency activities and because it will become progressively harder to make up lost ground.¹⁴⁶ Possible adaptations to permit continued implementation under difficulty include re-packaging contracts where feasible to permit local contractor implementation, thus lessening dependence on outside expertise, as well as promoting greater decentralized project implementation and supervision. Donors should also provide strong and consistent support for the PA's medium-term structural agenda as described in paras. 5.36-5.37 and 5.40-5.45 below.

Options for International Economic Relations and Trade

5.37 Looking to the future, WBG will need to develop its exports to take better advantage of its strategic geographical position, relatively open economy and preferential access to US and European markets (for industrial exports). Over the past few years export performance has been very poor, amounting to only some 17 percent of GDP in 2000.¹⁴⁷ At present, WBG exports are not competitive as a result of high transaction costs and limited access to the cheaper inputs available on world markets – a function of movement restrictions and a fiscal/trade regime featuring high import taxes on non-Israeli products, and a steep rate of VAT. A non-discriminatory trade regime would in theory lower the price of third country imports, which could in turn encourage a substitution of the export of labor to Israel by employment in the goods and services export sectors in WBG. Options for future economic relations with Israel include an improvement in the implementation of the de facto “customs union” established under the Paris Protocol of 1995, the creation of a Free Trade Area between WBG and Israel, and the development of a non-discriminatory Palestinian trade policy towards all other countries.¹⁴⁸

¹⁴⁶ In education, for example, the Five Year Education Plan includes \$45 million for expanding school capacity to absorb the natural growth in the number of new students.

¹⁴⁷ Compared with Jordan at over 40 percent of GDP.

¹⁴⁸ The periodic closure and restricted Palestinian access to Israeli labor markets cause major negative shocks to the Palestinian economy, and naturally raise the question of whether a strategy less reliant on the export of labor is feasible and could offer attractive growth opportunities. Promoting the exports of goods and services would be facilitated somewhat by the observed decline in Palestinian wages as a result of the closures of the past year. However, apart from the obvious fact that such a shift in policy could only occur with the support of Israel, success will require major improvements in the domestic investment climate as well as in the efficiency of trade administration, and new fiscal policies which improve the efficiency of public expenditure sufficiently to permit a

While these options are a matter for bilateral negotiation, the donors can usefully assist the discussions by exploring the technical advantages and disadvantages of the alternative policy structures.¹⁴⁹

PROPOSED ACTIONS BY THE PALESTINIAN AUTHORITY

5.38 The current crisis demands careful management of scarce Palestinian resources. The experience of the past year points to some areas in which improvements need to be made, something which holds true whether or not there is rapid political progress and a consequent economic recovery. In view of this and in response to the analysis and recommendations of the Assessment, the Palestinian Authority has worked with the World Bank to develop the text that follows in paras. 5.39–5.45, and has explicitly committed itself to what is presented below.

Coping with the Emergency: Expenditure Management, Planning and Aid Coordination

5.39 Improvements can be achieved in the following areas.

- *Maintaining Expenditure Discipline.* The Palestinian Budget for 2002 is being formulated so as to maintain the budget discipline in force since early 2001, when monthly outlays were cut by 17 percent from US\$107 million to an “austerity budget” of US\$90 million in recurrent expenditures. Arrears have now built up to an unsustainable level, and continued expansion is undesirable and no longer feasible, due to increasing supplier insolvency. Moreover, emergency spending associated with the current turmoil has crowded out non-wage expenditure. To maintain the budget ceiling without a further erosion of the non-salary budget, no net additional staff recruitment will take place as long as the current “austerity budget” is in force, with the exception of the hiring of a minimum number of teachers (needed to accommodate the annual expansion of enrollments at the beginning of the 2002/2003 school year), health workers and judicial employees.
- *Making Adequate Provisions for Operating Costs.* Despite the continuing fiscal crisis, a strong effort will be made to cover essential non-salary operating costs, since the price of not meeting them would be further decline in basic service delivery to the Palestinian people. To manage non-salary operating costs effectively, the Ministry of Finance will

reduction in taxes. Beside this, there would likely be significant short-term costs in terms of lower average incomes during a period of transition, and this would present political complications.

¹⁴⁹ The UK Government is currently supporting the third phase of the Economic Policy Programme (EPP3) with the Ministry of Economy and Trade through the London School of Economics. The project has been working to support MOET’s legal and technical capacity in trade negotiations with Israel, and is helping explore the costs, benefits and practicalities of alternative trade arrangements. The project is also helping the PA prepare for potential accession to the World Trade Organization. In another example, UNCTAD’s *The Palestinian Economy: Achievements of the Interim Period and Tasks for the Future*, March 2001, “suggests that Palestinian economic interests ‘may not be best served by negotiating a new trade relationship with Israel based on the current customs union’, whereby the Palestinian economy would adopt, and adapt to, most of the elements of the Israeli foreign trade regime, without reciprocal adjustment. Within this context the study stresses the importance of integrating the Palestinian economy and the rest of the world. However, such integration ‘can not be accomplished under the present conditions of infrastructure, institutional framework and supply constraints’.... As long as the Palestinian economy cooperates with its neighbors as the weaker and less proactive partner, this imbalance could perpetuate its current predicament.” UNCTAD Press Release, March 2001.

convene a monthly forum of the main spending ministries. Simple, transparent reporting formats will be devised and used in this forum, and protocols developed to ensure that resources can be moved flexibly between programs as needs evolve.

- *Developing an Emergency Plan.* The various sector crisis plans (such as those for the health and education sectors) will be drawn together into a Palestinian National Emergency Plan for 2002. MOPIC will lead this process, with close support from MOF and the Ministry of Economy and Trade (MOET). The World Bank, the IMF and other donors will be asked to assist in this effort. Municipalities and civil society will be fully involved in the exercise. The recurrent costs of the Plan will be kept consistent with the “austerity budget”. It is intended to prepare an initial draft of the Plan by the end of March 2002, and a full Plan by the end of April 2002. The Plan will serve as a guiding *framework*, within which implementing ministries and agencies will continue to detail out their activities with considerable freedom. Successful coping strategies employed so far will be lifted into the Plan.¹⁵⁰ The Plan will complement, not replace, the Palestinian Development Plan (PDP). Quarterly reviews of Plan implementation will be held to ensure active monitoring and a sharing of experiences.

- *Strengthening the core economic management institutions of the PA.* A concerted effort will be made to further develop the capacities of MOPIC, MOF and the Ministry of Economy and Trade (MOET). To equip the three ministries to meet current and future challenges, donors with interest and technical expertise are requested to help the PA develop a comprehensive program of capacity building, with monitorable benchmarks. Such a program should include, *inter alia*, (a) a re-definition and rationalization of functions, structures and staffing plans; (b) the full implementation of the Government Financial Information System; (c) the integration of recurrent and capital budgeting within the framework of a Medium Term Economic Framework,¹⁵¹ (d) the establishment of uniform procedures for the channeling of donor development funding to the PA; (e) regular production of the quarterly “donor matrix” of commitments and disbursements; and (f) support for long-term strategic policy formulation. As part of a comprehensive package of support, incentive structures will be reviewed in light of the current loss of qualified personnel, and necessary TA, equipment professional training will be requested from donors. A successful capacity-building experience with these three ministries could then lead to a more widespread program of institutional reform and strengthening.

Re-focusing on Structural Measures – the Medium-Term Policy/Institutional Agenda

5.40 The development of sound economic policies and effective public institutions with logical mandates was a major goal of the PA prior to the *intifada*, and a good deal of progress had been made by September 2000. The crisis put on hold most discussion of further policy and structural change, as the energies of the PA and donors alike were diverted into coping with the day-to-day. Some have argued that it makes little sense to focus at this stage on anything else,

¹⁵⁰ Such as the decentralization of line authority to district officials in the Ministries of Health and Education, which has helped them cope better with closure and movement difficulties.

¹⁵¹ The 2000 and 2001 budgets were prepared on the basis of a forward-looking macroeconomic framework, and initiated a process of gradual PA contribution towards the capital budget.

but the PA believes the opposite -- that extreme cash shortages, a decaying investment climate and serious impediments to implementation require greater budgetary efficiency, enhanced internal coordination and a better operating environment for the private sector, all of which were key issues on the structural agenda.

5.41 This agenda is reflected in a number of documents. Important commitments have been announced in the context of the Tripartite Action Plan, last signed in October 1999, and in the Economic Policy Framework, developed with IMF help and presented to the AHLC in June 2000. Other significant policy guidance is to be found in the “Rocard Report”,¹⁵² the World Bank’s 1999 public expenditure review¹⁵³ and the FIAS report of July 2001 on foreign investment prospects in WBG.¹⁵⁴ While these reports cover a wide range of governance issues, several themes pertinent to the management of the emergency and a possible recovery can be discerned. Attention will be given during 2002 to their further development and implementation.

5.42 **Promoting Transparency and Accountability on the Public Sector.** Measures to which the PA is strongly committed include:

- *Strengthening the financial control environment.* Priority actions include continued consolidation of all sources of revenue in a single treasury account, the sustained unification of the public payroll under the Ministry of Finance, the common application of public procurement standards and guidelines, and the strengthening of the capacity of the General Control Institution (the public audit entity).
- *Reviewing the organizational structure of the PA.* The roles, mandates and functions of all ministries and agencies will be given clear definition, with appropriate adjustments to eliminate overlap and redundancies.
- *Reforming the civil service.* The PA is committed to implement the reform agenda outlined by the Core Group on Public Administration (CGPA). In particular and at the right time following the current crisis, a program of civil service “down-sizing” will be developed in order to protect the fiscal position of the PA as well as allow “headroom” for improvements to the civil service salary and incentives structure. For this to be feasible, however, a unified pension system covering all public employees first needs to be developed; the PA has requested World Bank technical support for this, and work is underway. Another key issue for attention will be protecting merit-based recruitment and promotion.
- *Promoting plural service delivery.* The PA will help develop the capacity of the municipalities to deliver services by providing additional technical support for municipal budgeting and planning, and by promoting municipal budget rationalization.¹⁵⁵ Successful

¹⁵² *Strengthening Palestinian Public Institutions*, a report sponsored by the Council on Foreign Relations, June 1999.

¹⁵³ *Strengthening Public Sector Management*, World Bank, February 1999.

¹⁵⁴ The Foreign Investment Advisory Service of IFC: *Enhancing the Prospects for Foreign Direct Investment in West Bank and Gaza*, July 2001.

¹⁵⁵ The municipal agenda includes continued work on creating regional water and electricity utilities, and the disentangling the financing of utilities and municipal budgets; the regular transfer by MOF of centrally-collected

efforts at the sector level (e.g. health) to develop joint programming with NGOs and to contract them to deliver services in areas where they have comparative advantage will be extended to other service sectors. Periodic independent surveys of the quality of services delivered by different actors will be carried out and publicized widely.

- *Strengthening the social safety net.* The PA believes that protecting the poor and vulnerable is one of the major duties of any responsible government. At present the safety net available to the poor consists of a patchwork of public, UNRWA and NGO programs, many of which are effective, but which are incomplete in their coverage and are not always efficient. The planning and management of the PA's social welfare programs also needs improvement. The various schemes will be reviewed with a view to minimizing waste and avoiding neglect of any needy target group. Accordingly, as an initial step, the PA has asked for World Bank assistance in reviewing Palestinian social safety nets. A first mission has recently visited WBG and follow-up work will be undertaken within two months. Donors are encouraged to support capacity building for the Ministry of Social Affairs, including the development of an MIS that tracks all food and cash contributions being provided by donors and helps standardize criteria in use by the PA, UNRWA and NGOs.

5.43 Private Sector Support. Measures to which the PA is strongly committed include

- *Creation of an environment conducive to investment.* The large unused lending capacity of the domestic banking system (with a loan/deposit ratio of about 35 percent, compared with rates closer to 70 percent in most developing countries) reflects the high risk in WBG – and also some lack of confidence in the enabling environment. The PA is addressing this by presenting to the Palestinian Legislative Council (PLC) a number of laws which are in different states of preparation. These include the Capital Markets Authority Law, which was given its first reading in January 2002, the Insurance Law and Securities Laws, about to be introduced to the PLC as a joint package, a Companies Law, a Secured Financing (Leasing) Law¹⁵⁶ and an Income Tax Law. These various measures, once implemented, will help boost post-crisis investment flows.
- *Ensuring adequate competition.* The Economic Policy Framework was instrumental in the auditing of the Palestinian Commercial Services Company (PCSC) and the disclosure of its assets. The establishment of the Palestinian Investment Fund (to replace PCSC and oversee the privatization of PA assets, in particular the quasi-monopolistic trading activities) will be accelerated, and a Competition Law passed.¹⁵⁷
- *Promoting "economic legality".* The PA believes that the predictability of the legal system is vital, since investors must have confidence that contracts can be enforced and

revenues due to municipalities; improved efforts to raise local revenues; and the introduction of a "municipal equalization fund". The purpose of this would be to transfer funds to the poorer municipalities from a combination of central and local tax funds, so as to deliver similar levels of service for similar tax payments.

¹⁵⁶ This includes provisions for the establishment of a Register of Moveable Assets (RIMA), which would broaden the basis of assets against which loans can be contracted from commercial banks.

¹⁵⁷ The Competition Law would prevent monopolies and monopolistic practice in the public and private sectors, and contains provisions that outlaw price-fixing and collusion, and abuse of market position by large firms.

that they can be protected by the law. Accordingly, improvements will be made in the functioning of the court system, and the skills and independence of the judiciary will be enhanced. A suitable program has been laid out in detail in the Ministry of Justice's Rule of Law Strategic Development Plan.

5.44 It should be noted that such measures will not stimulate renewed investment unless there is certainty that a viable Palestinian state is being created. The severe and unpredictable oscillations between open borders and closures have demonstrated the resilience of the Palestinian private sector, but the PA believes they have largely dissuaded Palestinian and international entrepreneurs from investing again unless they can be sure that the long-term business environment is predictable and stable.

5.45 **Implementing the Reform Agenda.** The PA recognizes that statements of commitment to reform are of limited value unless they are implemented. Accordingly the PA will, by March 31, 2002, develop a detailed Action Matrix featuring the various reforms described above. The matrix will indicate who is responsible for a particular reform, the process involved in bringing it to a conclusion and the dates by which actions are to be taken.

IMMEDIATE PRIORITIES

5.46 Time, money and human resources are finite, and it is therefore important to indicate from the menus of actions proposed in this chapter a sub-set of top priority actions.

5.47 The most important contributions that *Israel* could make to economic recovery would be to

- Lift the system of internal and external closures, and once again permit Palestinians to enter Israel legally for work.
- Transfer the withheld revenue clearances, and resume monthly revenue transfers.

5.48 The *donors* would be well advised to focus on the following:

- Ensuring adequate support for the PA and municipal budgets.¹⁵⁸
- Revamping the collective welfare and job creation effort.
- Providing emergency support to the private sector.
- Pressing ahead with development-oriented investment and capacity building initiatives.

¹⁵⁸ As of early March 2002, the PA is facing a serious cash-flow problem. At the meeting of the Follow-Up Committee of the Ministers of Foreign Affairs of the Arab League in Damascus in November 2001, budget support of US\$55 million per month for the PA in 2002 was recommended, but no final commitment has yet been made (the Arab League Summit scheduled for late March in Beirut will consider the Committee's recommendation). Until then the PA will need to manage the unfunded deficit using a) the EU monthly contribution of 10 million Euros; b) advances on potential commitments by individual Arab League states (Saudi Arabia, for example, has agreed to pay US\$45 million over the three-month January-March period, equivalent to its share for the period); c) IDB project funds temporarily converted into budget support; and d) a Norwegian contribution of US\$10 million.

- Using the Sector Working Group structure to contribute to the design and implementation of Palestinian emergency programs.

5.49 The *Palestinian Authority* should take forward the commitments it has made in the following areas:

- Maintaining a disciplined expenditure program for 2002, with a monthly recurrent ceiling of US\$90 million.¹⁵⁹
- Completing, by April 30, the preparation of a Palestinian Emergency Plan for 2002, in full consultation with civil society.
- Completing, by March 31, an Action Matrix which assigns responsibilities and establishes dates for the structural program detailed above. This Action Matrix should take account of the measures proposed by the PA in the context of the EU's Direct Budget Assistance III Facility.¹⁶⁰
- Completing, with the assistance of the donor community, the design of a comprehensive program of capacity building for MOPIC, MOF and the Ministry of Economy and Trade.

¹⁵⁹ In a letter of January 21 2002 to the EU, the Minister of Finance confirmed a) that the PA had prepared a draft 2002 budget maintaining the austerity spending levels agreed with the IMF (US\$90 million per month). The letter also indicated b) that the budget for 2002 would shortly be considered by the Palestinian Legislative Council; c) that the PA would maintain the consolidation of all fiscal accounts under the Treasury; d) that there would be no further recruitment to the PA payroll in 2002 except for "absolutely necessary" education, health and judicial staff, and that the General Personnel Council in Gaza would continue to submit full details of the monthly payroll to the Ministry of Finance, highlighting and documenting each new recruitment; e) that MOF intended to apply any revenues in excess of minimum monthly requirements to the reduction of PA arrears; and f) that in accordance with the Organic Budget Law, the investment budget should be consolidated within the overall PA budget under the control of the Ministry of Finance.

¹⁶⁰ These measures include the promulgation of the Judiciary Independence Law by end-August 2002, the establishment of a ministerial-level body to monitor the implementation of the administrative reform program, and the release of an action plan to unify the different public sector pension schemes by en-September 2002.



ANNEXES

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ANNEX 1 STATISTICAL OVERVIEW OF THE WEST BANK AND GAZA ECONOMY

Poverty and social indicators

	2000
Population, mid-year (<i>millions</i>)	3.0
Gross national income per capita (current US\$)	1,716
GNI (current US\$ billion)	5.1
	1994-2000 or last available year
Average annual growth rate (<i>percent</i>)	
Population	4.6
Labor force	4.8
Poverty (<i>percent of population below national poverty line</i>)	23
Urban population (<i>percent of total population</i>)	54.0
Life expectancy at birth (<i>years</i>)	71.5
Infant mortality (<i>per 1,000 live births</i>)	15.0
Access to improved water source (<i>percent of population</i>)	90.0
Illiteracy (<i>percent of population age 15+</i>)	13.9
Gross primary enrollment (<i>percent of school-age population</i>)	97
Male	97
Female	96

Key economic ratios and long-term trends

	1999	2000
GDP (<i>US\$ billion</i>)	4.3	4.4
<i>Ratio to GDP</i>		
Gross domestic investment	37.3	30.2
Exports of goods and services	13.8	12.8
Gross domestic savings	-21.5	-24.2
Gross national savings	6.0	2.7
Current account balance	-36.5	-30.0
Total debt	7.3	9.0
<i>Annual real growth rate (percent)</i>		
GDP	7.2	-6.4
GDP per capita	3.0	-10.3
Exports of goods and services	3.3	-7.4

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Structure of the economy

	1999	2000
<i>Percent of GDP</i>		
Agriculture	8.3	8.0
Industry	28.5	26.5
Manufacturing	15.6	15.2
Services	63.2	65.5
<i>Private consumption</i>		
Private consumption	94.0	93.6
General government consumption	23.6	29.1
Imports of goods and services	73.5	70.0
<i>Annual real growth (percent)</i>		
Agriculture	3.6	-8.7
Industry	9.3	-11.8
Manufacturing	4.9	-7.7
Services	7.0	-5.3
<i>Private consumption</i>		
Private consumption	6.1	-6.7
General government consumption	9.7	15.5
Gross domestic investment	16.1	-19.0
Imports of goods and services	9.2	-10.9

Prices and government finance

	1999	2000
<i>Domestic prices (percentage change)</i>		
Consumer prices	5.5	2.7
<i>Government finance (percent of GDP, includes current grants)</i>		
Current revenue	28.0	28.2
Current budget balance	6.2	-0.6
Overall surplus/deficit	0.9	-4.6

Balance of payments

	1999	2000
<i>US\$ millions</i>		
Exports of goods and services	624.6	603.9
Imports of goods and services	3,367.8	3,085.8
Resource balance	-2,743.2	-2,481.9
<i>Net income</i>		
Net income	798.3	729.6
<i>Net current transfers</i>		
Net current transfers	378.9	443.0
<i>Current account balance</i>		
Current account balance	-1,566.0	-1,309.3

Note: Data exclude East Jerusalem.

Source: PA, World Bank staff estimates.

ANNEX 2

THE PALESTINIAN AUTHORITY'S FISCAL SITUATION AND PROSPECTS: IMF

The fiscal situation and prospects of the Palestinian Authority have worsened severely since the turmoil that broke out nearly a year ago. The adverse effects on the Palestinian Authority's fiscal position are transmitted through the sharp decline in its revenue-making capacity associated with the decline in economic activity and disruption in tax administration; the suspension by the Government of Israel of the transfer of the revenues it collects on behalf of the Palestinian Authority (the so-called clearance revenues); and the increase in expenditure associated with the emergency needs arising from the turmoil.

It is estimated that the Palestinian Authority's revenue-making capacity has dropped to about 60 percent of its pre-crisis level. This estimate is based on data on domestic revenue collection (revenues directly collected by the Palestinian Authority) for the period January–November 2001, estimated clearance revenue accrual during the same period, and actual data on both categories (domestic and clearance revenue) for the third quarter of 2000. Since the last clearance revenue transfer to the Palestinian Authority in late December 2000 up to end-December 2001, it is estimated the Government of Israel has accumulated, but withheld, about NIS 2.1 billion in clearance revenue.

It is difficult to determine the extent of the increase in expenditure associated with the emergency needs because of the difficulty of assessing the needs and corresponding pressures. However, a comparison of non-wage current expenditure trends before and after the crisis indicates a sharp drop from a monthly average of US\$54 million during the third quarter of 2000 to US\$31–34 million over the period April–November 2001. A substantial portion of this sharp reduction in monthly commitments (about 40 percent in 2001) was on account of emergency expenditure.

In late March 2001, the Palestinian Authority adopted a spending plan for April–September 2001 that sharply cut current expenditure commitments from a monthly average of US\$107 million during the third quarter of 2000 and a high of US\$110 million in December 2000 to about US\$90 million for April–November 2001. The plan projected average monthly revenues of US\$43 million (US\$16 million in domestic revenue collection and US\$27 million in clearance revenue transfers) and average monthly donor contributions of US\$46.5 million, thus ensuring a fully financed spending plan.

Over the period April–September 2000, current expenditure commitments, at about US\$90 million a month, were broadly in line with the plan. Domestic revenue collection, averaging US\$22 million a month, and donor budgetary support, at US\$48.5 million a month, were both slightly above projections.¹ The fiscal outcome for October and November 2001 was

¹ The international donor community provided direct budgetary support totaling US\$584 million during November 2000–December 2001: US\$460 million from Arab donors, bilaterally and multilaterally (Saudi Arabia

similar to that in April-September 2001. Contrary to a key assumption of the plan, the Government of Israel did not resume the transfer of Palestinian Authority clearance revenues. The resulting budgetary shortfall was reflected in the additional accumulation of domestic payments arrears, which stood at about US\$460-470 million at end-December 2001, compared with US\$155 million at end-December 2000. This forced credit from the private sector has resulted in an acute liquidity shortage, mounting non-performing loans in the banking system, and increasing cases of insolvency.

Looking ahead, the Palestinian Authority's fiscal outlook will largely be shaped by developments in the underlying political environment. Given the high degree of uncertainty in that environment, any projection of the Palestinian Authority's fiscal needs in the coming year has to be viewed with caution. With this important qualification in mind, it is estimated that the Palestinian Authority would need some US\$924 million in external budgetary assistance in 2002 if Israel does not resume the transfer of clearance revenues. If the transfers are resumed, the financing requirement would drop to about US\$600 million.

These projections are based on several assumptions:

- Continuation of the status quo in the performance of the Palestinian economy, with further erosion in the revenue base (to US\$15 million a month on the domestic revenue side and US\$27 million on the clearance revenue side).
- Continued ability to limit current expenditure commitments to a monthly average of US\$90 million and domestically financed capital expenditure to a monthly average of US\$1 million.
- No increase in the Palestinian Authority's net indebtedness to domestic banks. A budget for 2002 is currently being prepared with a monthly spending plan consistent with these expenditure limits and that precludes further arrears accumulation and borrowing from domestic banks, on the assumption that the required external financing will be forthcoming.
- No increase in domestic payments arrears.

and the United Arab Emirates provided US\$40 million and US\$15 million, respectively, in bilateral direct budgetary support to the Palestinian Authority, in addition to their contributions to multilateral support), US\$114 million from the European Union, and US\$10 million from Norway.

ANNEX 3

DAMAGE TO INFRASTRUCTURE, BUILDINGS, AND AGRICULTURE: WORLD BANK ESTIMATES

OVERVIEW

This annex provides additional details on damage to infrastructure, public buildings, private buildings, and agriculture in the West Bank and Gaza. Several points should be noted:

- The estimates are up to end-December 2001. However, damage has continued to occur almost daily since, especially to security-related public buildings, private homes, and agriculture.
- The estimates focus on physical *replacement costs* and do not include loss of earnings and other economic losses.
- Costs for *furniture and equipment* were estimated at an average rate of about 20 percent of construction cost estimates for *buildings*, which may understate the damage in some cases.
- The World Bank estimated the damage end-June 2001 and updated the estimates to December 2001 using recent data provided by the Ministries of Agriculture and Public Works (see below).
- Damage to *infrastructure* includes damage to *secondary roads* resulting from the forced diversion of normal traffic from primary roads—a significant factor in both West Bank and Gaza.

Table A3.1: Physical Damage Between September 28, 2000 and June 30, 2001, West Bank and Gaza

Sector	Amount (US\$ million)			Sectoral shares (percent)			Area shares (percent)		
	Gaza	West Bank	Total	Gaza	West Bank	Total	Gaza	West Bank	Total
Infrastructure	3	10.9	13.9	2	24	8	21	79	100
Agriculture	100.6	12.1	112.7	82	26	67	89	11	100
Public buildings	2.7	10.6	13.3	2	23	8	20	80	100
Private buildings	15.7	12	27.7	13	26	17	57	43	100
Total	122	45.6	167.6	100	100	100	73	27	100

Table A3.2: Physical Damage Between September 28, 2000 and December 31, 2001, West Bank and Gaza

<i>Sector</i>	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>
	US\$ million			Percent		
1. Infrastructure	12.7	27.4	40.1	7%	24%	13%
2. Agriculture	141.3	35.3	176.6	73%	31%	58%
3. Public buildings	16.7	24.1	40.8	9%	21%	13%
4. Private buildings	22	25.6	47.5	11%	23%	16%
Total	192.7	112.4	305.1	100%	100%	100%

DAMAGE TO AGRICULTURE: TREES, TOPSOIL AND STRUCTURES

The following tables give the unit costs estimates of damage to trees, topsoil and agricultural structures.

Table A3.3: Damage to Trees, Crops, Soil, and Structures, End-December 2001

	<i>Unit</i>	<i>Unit cost (US\$)</i>	<i>Number</i>	<i>Total (US\$)</i>
<i>Plant</i>				
Olives	Tree	250	155,343	38.84
Citrus	Tree	250	150,356	37.59
Almond	Tree	150	54,223	8.13
Forest	Tree	150	14,196	2.13
Date palm	Tree	1,000	12,505	12.51
Banana	Tree	50	18,400	0.92
Grapes	Vine	150	39,227	5.88
Other fruit	Tree	150	49,851	7.48
<i>Subtotal</i>			<i>494,101</i>	<i>113.47</i>
Structures ^a	Number	na	87,960	37.15
Rehabilitation of topsoil ^b	Dunum	800	32,467	25.97
Total				176.60

a. Includes agricultural storage buildings, barns, agricultural wells, water storage ponds, fences, and walls.

b. Damage to topsoil is assumed to be proportional to value of damage to trees.

OVERALL SUMMARIES

Table A3.4: Damage Assessment By Sector, End-June 2001

Sector	Amount (US\$ million)			Sectoral shares (percent)			Area shares (%)		
	Gaza	West Bank	Total	Gaza	West Bank	Total	Gaza	West Bank	Total
Infrastructure									
Roads (direct)	1.8	10.4	12.2	1	23	7	15	85	100
Roads (indirect)									
Transport									
Water and wells		0.3	0.3		1	0		100	100
Electricity	0.9	0.3	1.2	1	1	1	79	21	100
Telecommunications	0.2		0.2	0		0	100		100
Subtotal	3.0	10.9	13.9	2	24	8	21	79	100
Agriculture ^a	100.6	12.1	112.7	82	26	67	89	11	100
Public Buildings									
Education		3.7	3.7		8	2		100	100
Health		0.0	0.0		0	0		100	100
Local government		0.8	0.8		2	0		100	100
Social, cultural, religious		0.1	0.1		0	0		100	100
Other		6.1	6.1		13	4		100	100
Government	2.7		2.7	2		2	100		100
Subtotal	2.7	10.6	13.3	2	23	8	20	80	100
Special public ^b									
Subtotal	2.7	10.6	13.3	2	23	8	20	80	100
Private Buildings									
Residential	11.4	8.3	19.7	9	18	12	58	42	100
Commercial/industrial	4.3	1.7	6.0	4	4	4	72	28	100
Industrial		0.5	0.5		1	0		100	100
Tourism		1.6	1.6		3	1		100	100
Subtotal	15.7	12.0	27.7	13	26	17	57	43	100
Total	122.0	45.6	167.6	100	100	100	73	27	100

a. Agriculture re-estimated (topsoil and tree costs).

b. Includes the Gaza Airport and the West Bank Communication Building and facilities.

Table A3.5: Damage Assessment By Sector End-December 2001

<i>Sector</i>	<i>Amount (US\$ million)</i>			<i>Sectoral shares (percent)</i>			<i>Area shares (percent)</i>		
	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>	<i>Gaza</i>	<i>West Bank</i>	<i>Total</i>
Infrastructure									
Roads (direct)	2.0	7.9	9.9	1	7	3	20	80	100
Roads (indirect)	4.0	16.1	20.1	2	14	7	20	80	100
Transport	2.5	1.0	3.5	1	1	1	71	29	100
Water and wells	3.0	0.6	3.6	2	1	1	83	17	100
Electricity	0.9	1.7	2.7	0	2	1	35	65	100
Telecommunications	0.2		0.2	0		0	100		100
Infrastructure	0.1		0.1	0		0	100		100
Subtotal	12.7	27.4	40.1	7	24	13	32	68	100
Agriculture	141.3	35.3	176.6	73	31	58	80	20	100
Public Buildings									
Education		3.8	3.8		3	1		100	100
Health									
Local government		0.8	0.8		1	0			
Social, cultural, religious		0.1	0.1		0	0			
Other		6.0	6.0		5	2			
Government	8.4	8.2	16.6	4	7	5	51	49	100
Subtotal	8.4	18.9	27.3	4	17	9	31	69	100
Special public ^a	8.3	5.2	13.5	4	5	4	61	39	100
Subtotal	16.7	24.1	40.8	9	21	13	41	59	100
Private Buildings									
Residential	13.9	18.3	32.2	7	16	11	43	57	100
Commercial/industrial	5.9	1.7	7.7	3	2	3	78	22	100
Industrial		1.6	1.6		1	1		100	100
Tourism	2.1	4.0	6.1	1	4	2	34	66	100
Subtotal	22.0	25.6	47.5	11	23	16	46	54	100
Total	192.7	112.4	305.1	100	100	100	63	37	100

a. Includes the Gaza International Airport and the West Bank Communication Building and facilities.

GAZA SUMMARIES

**Table A3.6: Assessment of Damages By Sector and Governorate, Gaza, End-June 2001
(US\$ million)**

<i>Sector</i>	<i>North</i>	<i>Gaza</i>	<i>Middle</i>	<i>Khan Younis</i>	<i>Rafah</i>	<i>Total</i>
Infrastructure						
Roads (direct)		1.33	0.30	0.05	0.13	1.81
Roads (indirect)						
Transport						
Water and wells						
Electricity	0.09	0.36	0.17	0.14	0.18	0.93
Telecommunications		0.05	0.03	0.11	0.03	0.22
Infrastructure						
Subtotal	0.09	1.74	0.49	0.29	0.34	2.96
Agriculture ^a	33.52	18.23	25.83	14.91	8.13	100.62
Public Buildings						
Education						
Health						
Local government.						
Social, cultural, religious						
Other						
Government	0.49	1.98	0.06	0.05	0.08	2.66
Subtotal	0.49	1.98	0.06	0.05	0.08	2.66
Special public ^b						
Subtotal	0.49	1.98	0.06	0.05	0.08	2.66
Private Buildings						
Residential	0.68	3.98	1.08	2.14	3.50	11.38
Commercial/industrial	0.03	3.81	0.41	0.06	0.04	4.35
Industrial						
Tourism						
Subtotal	0.71	7.80	1.49	2.20	3.54	15.73
Total	34.81	29.75	27.87	17.46	12.09	121.97

a. Agriculture re-estimated (topsoil and tree costs).

b. Gaza International Airport.

Table A3.7: Assessment of Damages By Sector and Governorate, Gaza, End-December 2001 (US\$ million)

<i>Sector</i>	<i>North</i>	<i>Gaza</i>	<i>Middle</i>	<i>Khan Younis</i>	<i>Rafah</i>	<i>Total</i>
Infrastructure						
Roads (direct)	0.35	0.25	0.40	0.50	0.50	2.00
Roads (indirect)	0.70	0.50	0.80	1.00	1.00	4.00
Transport	0.08	0.32	0.06	0.03	1.99	2.48
Water and wells	0.37	0.20	0.25	0.30	1.90	3.02
Electricity	0.09	0.36	0.17	0.14	0.18	0.93
Telecommunications		0.05	0.03	0.11	0.03	0.22
Infrastructure	0.01	0.06				0.07
Subtotal	1.60	1.74	1.71	2.07	5.60	12.72
Agriculture	43.25	40.75	30.64	15.33	11.33	141.30
Public Buildings						
Education						
Health						
Local government.						
Social, cultural, religious						
Other						
Government	2.33	4.15	0.56	0.33	1.02	8.39
Subtotal	2.33	4.15	0.56	0.33	1.02	8.39
Special public ^a					8.30	8.30
Subtotal	2.33	4.15	0.56	0.33	9.32	16.69
Private Buildings						
Residential	1.37	2.69	3.03	2.43	4.40	13.92
Com/Industrial	0.02	5.45	0.42	0.04	0.02	5.95
Industrial						
Tourism		2.07		0.02		2.09
Subtotal	1.39	10.21	3.45	2.49	4.42	21.96
Total	48.57	56.85	36.36	20.22	30.66	192.66

a. Gaza International Airport.

WEST BANK SUMMARIES

Table A3.8: Assessment of Damages By Sector and Governorate, West Bank, End-June 2001 (US\$ million)

Sector	Jenin	Tubas	Tulkarm	Nablus	Qalqilyia	Salfit	Ramallah	Jericho	Jerusalem	Bethlehem	Hebron	Total
Infrastructure												
Roads (direct)	0.76	0.05	1.36	2.01	0.27	0.79	1.98	0.89	0.60	0.90	0.77	10.38
Roads (indirect)												
Transport												
Water and wells	0.01		0.11	Na	0.04			0.07			0.06	0.29
Electricity		0.00	0.13		0.04			0.03		0.01	0.05	0.25
Telecommunications												
Infrastructure												
Subtotal	0.77	0.05	1.61	2.01	0.35	0.79	1.98	0.99	0.60	0.91	0.87	10.92
Agriculture ^a	1.33	0.12	0.84		9.80							12.08
Public Buildings												
Education	0.02	0.00	3.49	0.02	0.00	0.00	0.06			0.05	0.02	3.66
Health				0.00		na	na	na		0.00	0.00	0.01
Local government.	0.07	0.00	0.58		0.01		0.09			0.06		0.81
Social, cultural, religious	0.00		0.00	0.04			0.01			0.04	0.01	0.11
Other			0.07	0.51		0.02	5.31	0.03		0.02	0.11	6.07
Government												
Subtotal	0.09	0.00	4.14	0.58	0.01	0.02	5.47	0.03		0.18	0.13	10.64
Special public ^b												
Subtotal	0.09	0.00	4.14	0.58	0.01	0.02	5.47	0.03		0.18	0.13	10.64
Private Buildings												
Residential	0.04	0.00	0.20	0.16	0.04	0.11	1.47	0.10	0.27	4.01	1.87	8.28
Commercial/industrial	0.05	0.01	0.14	0.02	0.45	0.07	0.11	0.04	0.00	0.44	0.34	1.67
Industrial	0.05		0.05		0.05					0.34		0.48
Tourism							0.80	0.01		0.74	0.01	1.56
Subtotal	0.13	0.01	0.38	0.18	0.53	0.19	2.38	0.15	0.28	5.53	2.22	11.99
Total	2.33	0.19	6.98	2.77	10.68	0.99	9.83	1.16	0.88	6.61	3.22	45.64

a. Agriculture re-estimated (topsoil and tree costs). b. Communication facilities in Ramallah.

Table A3.9: Assessment of Damages By Sector and Governorate, West Bank, End-December 2001 (US\$ millions)

<i>Sectors</i>	<i>Jenin/ Tubas</i>	<i>Tulkarem</i>	<i>Nablus</i>	<i>Qalqilia</i>	<i>Salfit</i>	<i>Ramallah</i>	<i>Jericho</i>	<i>Jerusalem</i>	<i>Bethlehem</i>	<i>Hebron</i>	<i>Total</i>
Infrastructure											
Roads (direct)	1.20	0.90	0.60	0.20	0.20	1.50	0.15	0.40	1.50	1.25	7.90
Roads (indirect)	2.00	1.20	2.20	0.60	0.60	2.20	0.90	0.80	2.60	3.00	16.10
Transport	0.03	0.17	0.02	0.01	0.06	0.05		0.03	0.38	0.28	1.03
Water and wells	0.05	0.12	0.01	0.17	0.01	0.08	0.01		0.06	0.10	0.61
Electricity		0.38		0.04	0.03	0.05	0.13		0.37	0.73	1.73
Telecommunications											
Infrastructure											
Subtotal	3.28	2.77	2.83	1.02	0.90	3.88	1.19	1.23	4.91	5.36	27.37
Agriculture	2.00	0.60	8.57	7.08	3.40	4.31	3.62	0.13	4.74	0.86	35.30
Public Buildings											
Education	0.02	3.49	0.02			0.16			0.05	0.04	3.78
Health											
Local government.	0.07	0.58		0.01		0.09			0.06		0.81
Social, cultural, religious			0.04			0.01	0.03		0.04	0.01	0.13
Other		0.07	0.51		0.02	5.31			0.02	0.11	6.04
Government	4.34	0.33	0.74	0.04	0.28	2.24	0.21				8.18
Subtotal	4.43	4.47	1.31	0.05	0.30	7.81	0.24		0.17	0.16	18.94
Special public ^a						5.20					5.20
Subtotal	4.43	4.47	1.31	0.05	0.30	13.01	0.24		0.17	0.16	24.14
Private Buildings											
Residential	0.63	0.81	0.16	0.22	0.43	2.24	0.10	0.27	7.44	6.01	18.31
Commercial/industrial	0.06	0.14	0.02	0.45	0.07	0.11	0.08		0.44	0.34	1.71
Industrial	0.05	0.05		0.05					0.77	0.65	1.57
Tourism						0.80	0.01		3.10	0.08	3.99
Subtotal	0.74	1.00	0.18	0.72	0.50	3.15	0.19	0.27	11.75	7.08	25.58
Total	10.45	8.84	12.89	8.87	5.10	24.35	5.24	1.63	21.57	13.46	112.39

a. Communication Facilities in Ramallah.

ANNEX 4 DAMAGE ASSESSMENTS BY THE PALESTINIAN AUTHORITY

Over the past year, the Palestinian Council for Development and Reconstruction, the Ministry of Finance, the Palestinian Ministry of Planning and International Cooperation, and other institutions of the Palestinian Authority have been undertaking comprehensive assessments of the damage caused by the current crisis. Although the methodologies, timeframes, and scopes differ, most of the assessments emphasize not only the overall economic losses caused by the *intifada*, but also the new constraints faced by the Palestinian Authority in responding to emerging needs and delivering vital services to the population.

This annex summarizes these assessments.

THE PALESTINIAN MINISTRY OF PLANNING AND INTERNATIONAL COOPERATION'S ASSESSMENT

Period

The period covered by this assessment is September 2000–December 2001.

Economical and Social Damages

Overall Economic Losses: US\$7.5 billion

- Housing: Destruction of 5,440 units in the West Bank, 5,400 in Gaza (28/9/00 – 28/9/2001). Estimated losses in national wealth: US\$541,888,000
- National Economy: GDP, GNP and labour compensations reduced by 33.1%; net income decline of 25.6%; Production output dropped to US\$732.5 million.
- Unemployment: 135,000 labourers were prevented from reaching the workplace inside the Green Line. Total unemployment reached 364,000 (54% of total manpower in Palestine). Daily losses due to labourers' unemployment are estimated at US\$7.28 million per working day.
- Losses in Taxes and VAT refunds: On the assumption that Israel used to transfer to the PA US\$55 million per month prior to the crisis, the total loss (budget deficit) has reached US\$524 million.
- International Contributions and Investments: Significant reduction in investment and available donor funding.
- Damage to Strategic Projects: Disruption of implementation of the power station project; damage to Gaza Airport (US\$16.6 million) and to the Gaza Seaport; cancellation of the Nablus-Jenin highway, etc.
- Human Losses: 876 Palestinian killed and 29,910 injured.

- Poverty: Based on UN definition of poverty line (\$2.1 per day), 2 million people are living below the poverty line. According to UNSCO, poverty rate at the end of 2000 had reached 42% and by August 15 2001 reached 64.2%
- Economic Sector Losses:
 - Industrial Sector: Production decreased by 65 percent [US\$761.2 million during the first year of *intifada*]
 - Agricultural Sector: Daily losses estimated at US\$224,000 [US\$496.7 million]
 - Trading Sector: Daily losses estimated at US\$265,600 and forgone opportunity estimated at US \$ 82,926. [US\$455.1 million]
 - Tourism Sector: [US\$385.3 million]
 - Health Sector: [US\$139.3 million]
 - Education Sector: 40 schools closed; 120,000 students prevented from reaching their schools; 542,123 students missed at least one day of school teaching during the first year of *intifada*.

THE MINISTRY OF FINANCE'S ASSESSMENT

Period

The period covered by this assessment is 28 September 2000–15 October 2001.

Macroeconomic Assumptions

The following macroeconomic assumptions underlie the assessment:

- Prior to the *intifada*, GNP growth was estimated at 6 percent in real terms for 2000.
- Economic losses result mainly from two Israeli policies:
 - Closures, including physical separation of cities and of West Bank and Gaza from Israel, delays in imports and exports of goods, and prevention of laborers from reaching their workplace.
 - Unilateral economic separation, including reestablishment of borders, control over border crossings, control of Palestinian exports to Israel according to Israeli priorities, prevention of movement of goods, non-transfer of tax revenues, and isolation of West Bank and Gaza from other Arab countries.

Estimated Losses

The following were the estimated losses:

A. Losses from weakening productive sector (US\$ million)	4,641
Agriculture (6 percent of GDP, 80 percent decline)	268
Mining, electricity, water, and manufacturing (18.2 percent of GDP, 62 percent decline)	620
Construction (12.1 percent of GDP, 80 percent decline)	532
Trade and commerce (11.11 percent of GDP, 50 percent decline)	305
Financial intermediation (2.99 percent of GDP, 25 percent decline)	41
Public administration (9.9 percent of GDP, 50 percent decline)	250
Social services (20 percent of GDP, 50 percent decline)	555
Tourism and other (16.2 percent of GDP, 90 percent decline)	800
Remittances and other	1,270
B. Damages to national wealth (US\$ million)	922
<i>Agriculture</i>	268
Uprooting of 375,000 evergreen fruit trees	
Destruction of irrigation networks, greenhouses, farms	
<i>Housing and government buildings</i>	199
Destruction of 5,000 units (private houses, hospitals, public buildings)	
<i>Industrial installations</i>	91
<i>Infrastructure</i>	86
Roads, sanitary/water networks, telephone lines, generators	
<i>Transportation</i>	43
Private and public vehicles (incl. ambulances)	
<i>Lost investment opportunities</i>	235
C. Human losses	
• 750 Palestinians killed (average age: 22 years)	
• 33,000 Palestinians injured (20 percent with permanent disabilities)	
• 2,000 Palestinians arrested.	
D. Additional burdens to the national economy (US\$ million)	875
Health sector	235
Security	202
Social services	118
Education	35
Increased import costs	61
Supplies	41
Infrastructure	71
Cash support to unemployed workers	108
Assistance to owners of destroyed houses	1.5
Assistance to farmers	1.8
Assistance to owners of destroyed factories	1

E. Losses resulting from additional burden to the budget (US\$ million)	50
F. Palestinian Authority revenues withheld by Israel (US\$ million)	380
G. Direct impact on the treasury (US\$ million)	1,500
Decline in revenue during the fourth quarter of 2000	200
Decline in revenue in first half of 2001	425
Increase in financial burden	875
Support of dependents of those killed, handicapped, detained	85

Table A4.1: Summary of Losses to Palestinian Economy, Ministry of Finance Estimate, 28 September 2000–15 October 2001

<i>Losses</i>	<i>Amount (US\$ million)</i>
A. Recurrent losses in productive sector	4641
B. National wealth	922
D. Additional economic burdens	875
E. Additional budget burdens	50
F. Revenues withheld by Israel	380
G. Support of dependents	85

Total Losses: US\$6.953 billion

THE MINISTRY OF SOCIAL AFFAIRS' ASSESSMENT

Main Findings

The following were the main findings of the assessment:

- A substantial increase in the Ministry of Social Affairs' financial responsibilities as a result of increased poverty, increased number of needy people, and inability of workers to reach their workplace.
- An increase in unemployment to about 60 percent (highest unemployment rates are in Gaza). Some 135,000 workers could not reach their workplaces inside the Green line, and 70,000 workers were already unemployed before the *intifada* (see Table A4.2). Estimated daily losses of around US\$42 million. Local factories and workshops suffering, leading to a substantial increase in assistance requests.
- Delayed transfers of funds from the Palestinian Authority to the Ministry of Social Affairs causing delays in providing monthly assistance to social service clients.
- Lower quality and quantity of food supply assistance to needy families.
- Decreased ability to provide cash assistance because of the separation of areas within the West Bank and Gaza.
- Increase in staff (in particular social workers) needed to respond to emerging needs.

- Required increase in the budget for the families of those killed and injured, as well as an increase in economic and vocational rehabilitation opportunities and the opening of new centers. In addition to the 600 Palestinians who had already died because of the crisis and the 25,000 who had been injured, thousands will suffer from permanent disabilities.

Table A4.2: Workers and Families in Need of Urgent Assistance, Ministry of Social Affairs Estimate

<i>Category</i>	<i>Number</i>
Unemployed workers who used to work in Israel	120,000
Unemployed workers in industrial zones and Israeli settlements	15,000
Unemployed workers before the current <i>intifada</i>	70,000
Unemployed workers due to the current economic deterioration	120,000
<i>Subtotal</i>	<i>325,000</i>
Families obtaining assistance from Ministry of Social Affairs (difficult cases)	45,000
Families obtaining assistance from Ministry of Social Affairs (difficult cases but not registered permanently due to lack of budget)	20,000
Families of unemployed workers	20,000
<i>Total number of families in need of assistance</i>	<i>410,000</i>

THE MINISTRY OF HEALTH'S STRATEGY, 12 JULY 2001

The Ministry of Health did not make an independent assessment of the impact of the *intifada* on its operations. Instead, it adopted an emergency strategy for coping with the ongoing crisis, which included the following activities:

- Decentralize services.
- Strengthen community participation in health services.
- Strengthen telecommunications among West Bank, Gaza, and Jerusalem.
- Consolidate cooperation among the Palestinian Authority, the UN Relief Works Agency for Palestine Refugees (UNRWA), Palestine Red Crescent Society (PRCS), community organizations, and NGO health providers.
- Upgrade emergency medical services.
- Improve community mental health services for school children, women, and university students.
- Improve rehabilitation services for the handicapped.
- Expand the scope of cooperation with Arab and friendly foreign countries, at official and NGO levels.

MINISTRY OF PLANNING AND INTERNATIONAL COOPERATION'S IMMEDIATE AND SHORT-TERM ACTION PLAN, JANUARY 2001

The Ministry of Planning and International Cooperation prepared an immediate and short-term action plan in response to the economic impacts of the crisis and its effects on Palestinian institutions.

Economic Impacts of the Crisis

The Ministry of Planning and International Cooperation estimated losses to the Palestinian economy from the crisis at US\$1.25 billion as of January 2001. The Israeli-imposed closure preventing Palestinian laborers from reaching their workplaces in Israel drove unemployment up to 40 percent. Trade restrictions on Palestinian imports of raw materials and exports of agricultural and nonagricultural products forced many factories to close. Tourism had come to a halt.

Effects on Palestinian Authority Institutions

The Israeli closures prevented many Palestinian Authority staff from reporting to work, hampering the operation of vital activities, including education and health care. The Palestinian Authority had lost over 12.5 percent of its revenues (approximately US\$100 million).

Palestinian Needs

The Ministry estimated the following needs, by sector:

- *Health:* Shortages of medicines, equipment, and supplies in hospitals; qualified health care personnel; and rehabilitation centers. The absence of health care centers in rural communities was detrimental to the well-being of many Palestinians living in these communities.
- *Education:* New priorities included distance learning, alternative educational sites, new school construction, expansion of existing schools, and rehabilitation of damaged schools.
- *Agriculture:* Rehabilitation of destroyed farm land, compensation for farmers who had lost produce or livestock, and replanting of uprooted trees.
- *Industry:* Need to rebuild factories and to provide compensation for the losses incurred because of the closures (restricted mobility of goods, storage fees, and the like).
- *Private sector:* High default rate on commercial loans; higher dependency on locally produced products, generating a need for technical assistance in improving quality.

MINISTRY OF PLANNING AND INTERNATIONAL COOPERATION'S ASSESSMENT, SEPTEMBER– DECEMBER 2000

Table A4.3: Summary of Losses to Palestinian Economy, Ministry of Planning and International Cooperation Estimate, End-December 2001

<i>Loss</i>	<i>Amount (US\$ million)</i>
Economic losses	13.3/day
Losses to the local economy	284.8
Investment opportunities lost	401.06
Long-term losses	196.43

Productive Sector

- *Trade:* Closures have caused significant reduction in trade, and profits for the private sector have decreased along with income to the treasury (value-added tax). Unemployment in the private sector has increased. Delays in ports and airports have raised costs substantially.
- *Industry:* Industry has suffered from inaccessibility to raw materials (mostly from Israel), which has greatly hurt output. Twenty factories have been destroyed, and more than 100 factories have been damaged. The largest impact has been the loss of markets because of the inability to delivery goods on time.
- *Agriculture:* Israeli agriculture is based on a seven-year cycle, with the land left fallow in the seventh year. Since crop year 2000/01 is the fallow year, Palestinian farms would normally have supplied up 45 percent of Israel's demand for agricultural goods. Palestinian farmers had planned for this level of demand, but the closures have prevented them from delivering products to Israeli markets. There has also been heavy destruction of topsoil and uprooting of trees (23,000 trees up to the first week of November). Tree replacement costs (US\$ per tree) are estimated as follows:

Olive	\$114
Small trees	\$41
Citrus	\$180
Almond	\$419
Palm	\$264
Banana	\$19
Grape	\$69
Forest tree	\$1.6

- *Fisheries:* US\$150,000 worth of fish spoiled while waiting to be exported to Israel. Fishing activity has been reduced by 35 percent.

Services

- *Tourism:* Cancellation of all reservations. Loss of 65 percent of jobs. Destruction or occupation of three hotels. Drastic reduction in investment. Total cessation of internal tourism.
- *Transportation:* Loss of revenue resulting from transporting 80,000 workers in and out of Israel. Reduction of transportation activity by 55 percent. Loss of jobs for 5,400 taxi drivers.
- *Communications:* International communications reduced by 35 percent. Internal phone calls reduced by 60 percent. Total losses of US\$30 million a month. Physical damage estimated at US\$3.4 million.
- *Banking:* Large transactions (greater than US\$1 million) decreased from 25 to 2 a day. Hard currency transfers abroad have increased by 180 percent. Workers' income reduced by 16 percent.
- *Stock market:* A 40 percent decline in market capitalization, 18 percent decline in volume of trade, and 60 percent decline in daily transactions.

Strategic Projects

- *Airport:* Closure of airport resulted in losses estimated at US\$7 million a month (Palestinian Airlines and services provided to other airlines)
- *Port:* The construction company invoked *force majeure*, requesting US\$3 million (US\$43,000 a day). Forgone revenue of US\$2.5 million a month.
- *Power station:* *Force majeure* clause costs US\$1 million a month. Equipment blocked in Ashdod port costs US\$5,200 a day in storage fees. Forgone revenue of US\$1.1 million a day in sales.
- *Industrial estates:* Important projects have been frozen: Rafah IE project (US\$40 million), Khadouri IE (US\$65 million), second stage of Gaza IE (US\$21 million), Jenin IE (US\$21 million), and Nablus IE (US\$26 million).

Construction, Housing, and Cement

- *Construction and housing:* Physical destruction of buildings and houses, halt in further investment, high losses by construction companies and engineering firms.
- *Cement:* Lack of cement, mostly imported from Israel, caused delay in construction works, with total loss estimated at US\$230 million. Cement price increased from NIS 330 to NIS 650 a ton.

Workers Employed in Israel

- 120,000 workers earning NIS 140 a day have been prevented from reaching their work.
- 53 percent of workers were not paid their salary the week of 28 September, 2000 (US\$14.1million).

Investment

- Many foreign companies left the country (industry, US\$31.5 million; agriculture, US\$8.6 million; infrastructure, US\$1.6 million; services, US\$7.8 million).
- Cancelled investments: Nestlé, JTI, and one diamond factory (GIE), US\$27 million; Pepsi and Coca-Cola, US\$7 million; Aqad Group, US\$3.6 million; Click (Jordan Telecom), US\$12 million; agriculture, US\$6.2 million.
- Total: US\$55.8 million.

Social Sectors

- *Education:* Average time to complete university studies will increase by 15 percent for 50,000 students.
- *Health:* See Main Report on numbers of dead and injured.
- *Legislation:* Palestinian Legislative Council could not meet throughout the period of crisis.

OFFICE OF THE PRESIDENT - DAMAGES AND COMPENSATION COMMITTEE

Table A4.4: Summary of Compensation Needed From International Development Banks for September 28, 2000–September 2, 2001 (US\$ million)

Governorate	Installment	Agriculture	Buildings	Industry	Infra-structure	Trade and Economy	Tourism	Transport	Total
North Gaza	1	5.81						0.01	5.82
	2								0.00
	3	7.52							7.52
	4	2.90		0.60					3.50
	5	0.57							0.57
Total		16.80	0.60	0.00	0.00	0.00	0.00	0.01	17.41
Gaza	1	4.80		1.96			2.07	0.28	9.11
	2	5.11	3.15		0.05			0.00	8.31
	3	0.65	0.05						0.70
	4	1.10	0.74	1.04				0.02	2.90
	5	3.53	0.12	1.03			0.05		4.73
Total		15.19	4.06	4.03	0.05	0.05	2.07	0.30	25.75
Middle	1	11.00	1.11	0.42				0.00	12.53
	2	1.40	0.26					0.00	1.66
	3								0.00
	4								0.00
	5								0.00
Total		12.40	1.37	0.42	0.00	0.00	0.00	0.00	14.19
Khan Younis	1	2.76	0.98					0.02	3.76
	2		0.94					0.00	0.94
	3	2.30							2.30
	4								0.00
	5	1.70	0.04	0.02			0.01		1.77
Total		6.76	1.96	0.02	0.00	0.01	0.00	0.02	8.77
Rafah	1	3.23						2.00	5.23
	2	0.60	0.41						1.01
	3	0.70	0.22						0.92
	4	0.55	1.06			0.10			1.71
	5							0.00	0.00
Total		5.08	1.69	0.00	0.00	0.10	0.00	2.00	8.87
TOTAL GAZA		56.23	9.68	4.47	0.05	0.16	2.07	2.33	74.99

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Hebron	1		0.03			0.03		0.06	
	2	0.00						0.00	
	3		2.40		0.05		0.30	2.75	
	4	0.36						0.36	
	5				4.50	0.00		4.50	
Total		0.36	2.43	0.00	4.55	0.00	0.03	0.30	7.67
Bethlehem	1		0.12	0.25			0.42	0.79	
	2						0.01	0.01	
	3		3.51				0.19	3.70	
	4	0.70	1.16				0.01	1.87	
	5		1.02				0.15	1.17	
Total		0.70	5.81	0.25	0.00	0.00	0.42	0.36	7.54
Ramallah and Al Birch	1					0.12	0.12	0.02	0.26
	2							0.00	
	3	1.80	7.15				0.03	8.98	
	4	0.10					0.00	0.10	
	5					0.41		0.41	
Total		1.90	7.15	0.00	0.00	0.53	0.12	0.05	9.75
Jerusalem	1							0.00	
	2							0.00	
	3		0.30				0.03	0.33	
	4	0.04						0.04	
	5							0.00	
Total		0.04	0.30	0.00	0.00	0.00	0.00	0.03	0.37
Jericho	1							0.00	
	2							0.00	
	3							0.00	
	4	0.50						0.50	
	5					0.03	0.20	0.23	
Total		0.50	0.00	0.00	0.00	0.03	0.20	0.00	0.73
Nablus	1							0.00	
	2	0.20						0.20	
	3		0.51				0.02	0.53	
	4	2.40						2.40	
	5							0.00	
Total		2.60	0.51	0.00	0.00	0.00	0.00	0.02	3.13
Salfect	1							0.00	
	2							0.00	
	3		0.13		0.05		0.06	0.24	
	4	0.40						0.40	
	5							0.00	
Total		0.40	0.13	0.00	0.10	0.00	0.00	0.06	0.69

Fifteen Months – Intifada, Closures and Palestinian Economic Crisis – An Assessment

Tubas	1								0.00
	2								0.00
	3		0.62		0.21			0.01	0.84
	4	0.10	0.00					0.00	0.10
	5								0.00
Total		0.10	0.62	0.00	0.21	0.00	0.00	0.01	0.94
Qalqilia	1								0.00
	2								0.00
	3		0.22		0.00			0.01	0.23
	4	1.54		0.01					1.55
	5			0.00		0.04			0.04
Total		1.54	0.22	0.01	0.00	0.04	0.00	0.01	1.82
Tulkarem	1				0.60				0.60
	2								0.00
	3		4.00		0.40			0.03	4.43
	4	0.25	0.04	0.16	0.30	0.12	0.10	0.14	1.11
	5				0.20				0.20
Total		0.25	4.04	0.16	1.50	0.12	0.10	0.17	6.34
Jenin	1		0.01						0.01
	2			0.05					0.05
	3		0.12					0.00	0.12
	4	0.80		0.11		1.11		0.02	2.04
	5								0.00
Total		0.80	0.13	0.16	0.00	1.11	0.00	0.02	2.22
TOTAL WEST BANK		9.19	21.34	0.58	6.36	1.83	0.87	1.03	41.20
Grand Total		65.42	31.02	5.05	6.41	1.99	2.94	3.36	116.19

ANNEX 5

THE IMPACT OF THE CRISIS ON MUNICIPAL FINANCES: WORLD BANK ESTIMATES

The estimates of the impact of the crisis on municipal finances in the West Bank and Gaza are based on municipal samples in both areas, 10 in the West Bank and 4 in Gaza. The data cover the four quarters prior to October 2000 (the pre-*intifada* period, Q4 1999 and Q1-3, 2000) and the three subsequent quarters (the post-*intifada* period, Q4 2000 and Q1-2, 2001).

IMPACT ON MUNICIPAL FINANCES IN THE WEST BANK

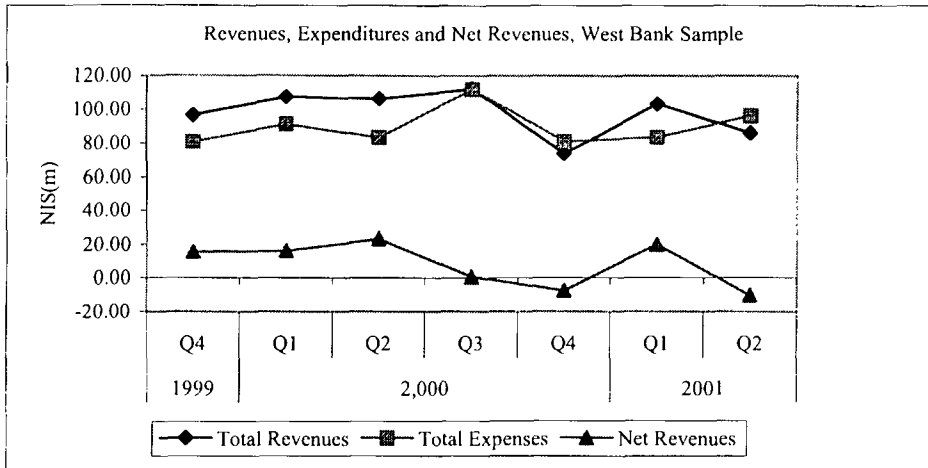
The findings on the impact of the *intifada* on the finances of West Bank municipalities are based on a sample of 10 municipalities: Jenin, Qalqilia, Nablus, Anapta (north), Ramallah, Al Bireh, Bethlehem, Jericho (central), Hebron, and Dura (south). Together, they account for approx. 25 percent of the population of the West Bank and 40–50 percent of municipal revenues and expenditures.

The municipalities vary considerably in population. Nablus and Hebron are large towns with populations of 130,000-150,000. Jenin, Qalqilia, Ramallah, Al Bireh Jericho, Bethlehem, and Dura are mid-size towns with 20,000-35,000 people, while Anapta is a small town with a population of about 7,000-8,000.

The municipalities also vary considerably in revenues and expenditures. Nablus has annual revenues and expenditures of over NIS 150 million and Hebron of over NIS 80 million. Jenin and Qalqilia have annual revenues and expenditures in the NIS 20-30m range; Al Bireh and Ramallah in the NIS 15-20 million range; and Bethlehem, Jericho, and Anapta in the NIS 3-9 million range. On a per capita basis, Nablus is the wealthiest (NIS 1,500), followed by Ramallah and Jenin (NIS 1,100) and Hebron and Qalqilia (NIS 700). Bethlehem and Jericho are at the bottom of the group (NIS 400), and next to last are Al Bireh and Anapta (NIS 500).

The municipalities also differ in level of service provision. For example, Ramallah, Al Bireh, and Bethlehem do not provide electricity and water services; Jericho does not provide electricity; and Dura and Anapta do not provide wastewater services. These variations must be considered in reviewing the data presented here.

Figure A5.1: Municipal Revenues, Expenditures, and Net Revenues Before and After the Start of the Intifada in October 2000, West Bank Sample



Overall Financial Position

Despite a number of concerns about the reliability of the data, it is clear that the *intifada* has seriously harmed municipal finances (see summary in figure A5.1). In particular:

- Municipalities have experienced a general decline in revenues of about 17 percent on an average period to period basis between the pre-*intifada* period and the subsequent period.
- The decline has been accompanied by a large increase in arrears in payments due from customers.
- The decline in revenues has forced municipalities to reduce expenditures, though not by as much as the reduction in revenues. Expenditures fell by about 5 percent on an average period to period basis. Expenditures were reduced mainly by reducing services, increasing liabilities to staff, and increasing liabilities to suppliers.

A key area of services reduction has been solid waste collection and disposal. This service accounts for the highest share of utility expenditures, which have historically exceeded corresponding revenues. These account for the largest deficits among utilities and overall. Waste collection and disposal services also account for the largest share of municipal staffing and equipment. Service reduction has taken the form of less frequent collection and disposal, significantly increasing the buildup of garbage in urban areas. The potentially harmful environmental and public health consequences are obvious.

Electricity services have also been reduced in some municipalities, in particular in Nablus.

Liabilities are especially high in electricity and water. Both involve increasing liabilities to Israeli public utility suppliers, often exceeding three months. The buildup of liabilities to staff is also highly problematic and has led to protests in some municipalities, in particular in Bethlehem. Available data on liabilities probably understate the true position.

Revenues

Figure A5.1 and Table A5.1 summarize revenues for the West Bank sample for periods before and after the beginning of the *intifada*. Revenues fluctuated considerably. In the pre-*intifada* period revenues peaked at NIS 112.5 million in the third quarter (Q3), just before the start of the *intifada*. Thereafter, revenues fell dramatically, by 35 percent, in the first quarter of the *intifada*, to NIS 74 million, recovered in the following quarter to NIS 103 million as municipalities took measures to arrest the decline, mainly by increasing collections; and then fell again, by 15 percent, to NIS 86 million in the last quarter for which data were collected (Q2 2001), seemingly reflecting an exhaustion of the collection drive. On an average period to period basis, municipalities lost 17 percent of their revenues since the beginning of the *intifada*.

Table A5.1: Municipal Revenues in Period Before and After Start of the Intifada in October 2000, West Bank Sample (millions of NIS)

	Q4	Q1	Q2	Q3	Period Average
Pre- <i>intifada</i>	96.4	107.4	106.4	112.5	105.7
Post- <i>intifada</i>	73.7	103.3	86.1	na	87.7
Percentage change, pre- to post- <i>intifada</i>	-24	-4	-19	na	-17

Expenditures

Expenditures peaked at NIS 112 million in the quarter before the beginning of the *intifada*; fell by about 28 percent in the first quarter of the *intifada* (Q4 2000), to NIS 81 million; rose slightly in the following quarter; and rose again, by 15 percent, to NIS 96 million in Q2 2000, apparently in response to increased pressures for services arising from the *intifada*. The average period to period decline was about 5 percent. Expenditures were below revenues for most of the pre-*intifada* period, equaled revenues in the quarter just before the *intifada*, and were above revenues in two of the three post-*intifada* quarters (see figure A5.1).

Table A5.2: Municipal Expenditures in Period Before and After Start of the Intifada in October 2000, West Bank Sample (millions of NIS)

	Q4	Q1	Q2	Q3	Period Average
Pre- <i>intifada</i>	80.9	91.3	83.3	112.0	91.9
Post- <i>intifada</i>	81.1	83.4	96.2	na	86.9
Percentage change, pre- to post- <i>intifada</i>	0	-9	16	na	-5

Net Revenues

Net revenues were significantly positive in the pre-*intifada* period but were beginning to show an increasingly negative trend just before the outbreak of the crisis (see Figure A5.2 and Table A5.3). Net revenues were slightly positive in Q3 2000, but fell dramatically by almost 150 percent to minus NIS 7.4 million in the first quarter of the *intifada*, recovered significantly to about NIS 20 million in the next quarter, and became significantly negative again (minus NIS

10 million) in Q2 2001, the last quarter for which data were collected. On an average period to period basis, the deficit has increased by 94 percent since the beginning of the *intifada*.

Table A5.3: Municipal Net Revenues in Period Before and After Start of the Intifada in October 2000, West Bank Sample (millions of NIS)

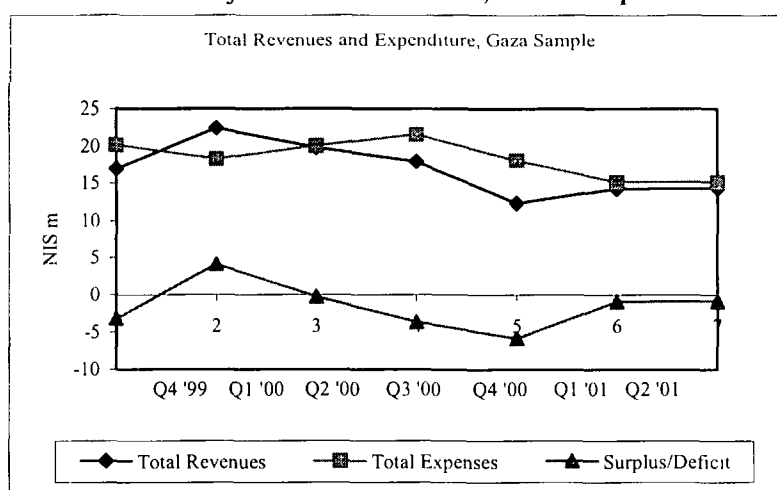
	Q4	Q1	Q2	Q3	Period Average
Pre-intifada	15.5	16.1	23.1	0.5	13.8
Post-intifada	-7.4	19.8	-10.2	na	0.8
Percentage change, pre- to post-intifada	-148	23	-144	na	-94

IMPACT ON MUNICIPAL FINANCES IN GAZA

The findings on the impact of the *intifada* on the finances of Gaza municipalities are based on a sample of four municipalities: Gaza City, Rafah, Khan Younis, and Beit Hanoun. Together, they account for about 60 percent of the Gaza population and 60-70 percent of municipal revenues and expenditures.

As in the West Bank, the municipalities vary considerably in population and revenues. Gaza municipality, with a population of 300,000 is by far the largest, accounting for almost 40 percent of the total municipal population and 50 percent of annual revenues and expenditures. Khan Younis’s population is about 100,000, and it accounts for about 10-12 percent of total municipal revenues and expenditure. Rafah and Beit Hanoun have about 30,000-50,000 people, but Rafah accounts for about 8 percent of total municipal revenues and expenditures, while Beit Hanoun accounts for 2 percent. On a per capita basis, revenues range from about NIS 120 in Beit Hanoun to about NIS 170-190 in Gaza and Rafah. These variations must be considered in reviewing the data presented here.

Figure A5.2: Municipal Revenues, Expenditures, and Net Revenues Before and After the Start of the Intifada in October 2000, Gaza Sample



Overall Financial Position

Despite a number of concerns about the reliability of the data, it is clear that the *intifada* has had a serious negative impact on municipal finances (see summary in Figure A5.2). In particular:

- Municipalities have experienced a general decline in revenues of about 30 percent on an average period to period basis between the pre-*intifada* period and the subsequent period.
- The decline has occurred in three main revenue categories: taxes, down 44 percent; local services, down 30 percent; and utilities, down 21 percent on an average period to period basis. The declines have been accompanied by a large increase in arrears in payments due from customers.
- The decline in revenues has forced municipalities to reduce expenditure, though not by as much as the reduction in revenues. Expenditures fell by about 19 percent on an average period to period basis. The reductions in expenditure have been achieved mainly by reducing services, increasing liabilities to staff, and increasing liabilities to suppliers.

A key area of services reduction has been solid waste collection and disposal. This service accounts for the highest share of utility expenditures, which have historically exceeded corresponding revenues. These account for the largest deficits among utilities and overall. Waste collection and disposal services also account for the largest share of municipal staffing and equipment. Service reduction has taken the form of less frequent collection and disposal, significantly increasing the buildup of garbage in urban areas. The potentially harmful environmental and public health consequences are obvious.

Liabilities are especially high in electricity and water. Both involve increasing liabilities to Israeli public utility suppliers, often exceeding three months. Available data on liabilities probably understate the true position.

Revenues

Figure A5.2 and table A5.4 summarize revenues for the Gaza sample for periods before and after the beginning of the *intifada*.

Table A5.4: Municipal Revenues in Period Before and After Start of the *Intifada* in October 2000, Gaza Sample (millions of NIS)

	<i>Q4</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3</i>	<i>Period Average</i>
Pre- <i>intifada</i>	17.0	22.5	19.8	18.0	19.3
Post- <i>intifada</i>	12.3	14.2	14.3	na	13.6
Percentage change, pre- to post- <i>intifada</i>	-9	-35	-44	na	-30

Revenues fluctuated throughout. In the pre-*intifada* period, revenues peaked at NIS 22.5 million (Q1 2000), probably reflecting annual tax collections during this period. They declined to about NIS 18 million in the quarter just before the start of the *intifada* (Q3 2000); fell dramatically, by 31 percent, in the first quarter of the *intifada* to NIS 12.3 million; recovered to some extent in the following quarter; and then appeared to stabilize at around NIS 14 million as

municipalities took measures to arrest the decline (mainly by increasing collections). On an average period to period basis, municipalities lost about 30 percent of revenues since the beginning of the *intifada*.

Expenditures

Expenditures also fluctuated, though less than revenues (see Figure A5.2 and Table A5.5). Expenditures peaked at about NIS 21.6 million in the quarter before the start of the *intifada*; fell by about 16 percent in the first quarter of the *intifada* (Q4 2000), to NIS 18.1 million; fell again in the following quarter; and appeared to stabilize at about NIS 15 million. The average period to period decline was about 19 percent. Expenditures exceeded revenues for most of the period under review.

Table A5.5: Municipal Expenditures in Period Before and After Start of the *Intifada* in October 2000, Gaza Sample (millions of NIS)

	<i>Q4</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3</i>	<i>Period Average</i>
Pre- <i>intifada</i>	20.2	18.3	20.1	21.6	20.0
Post- <i>intifada</i>	18.1	15.2	15.2	na	16.14
Percentage change, pre- to post- <i>intifada</i>	-10	-17	-24	na	-19

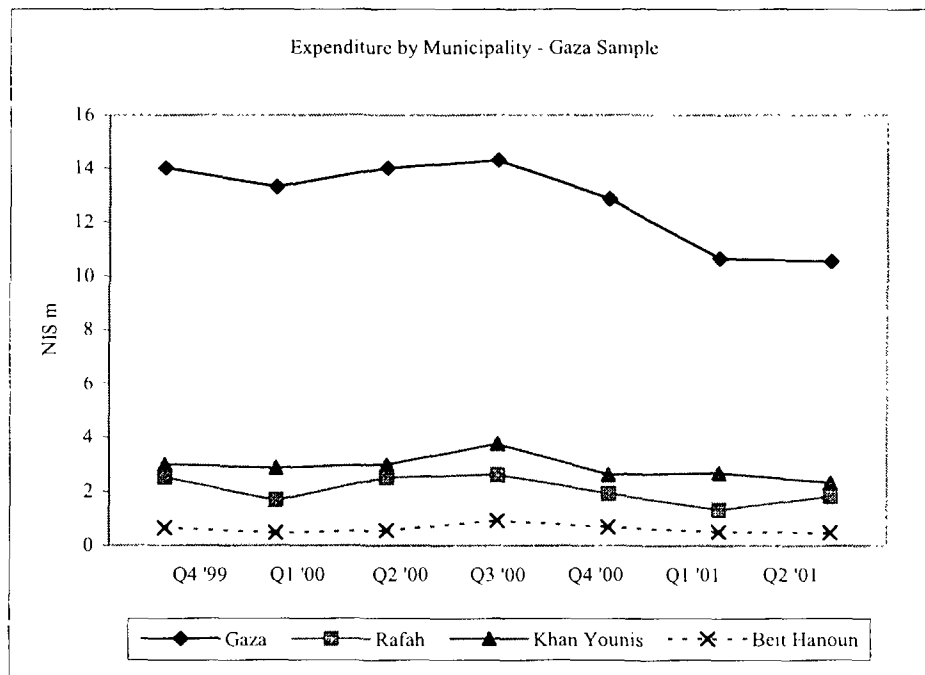
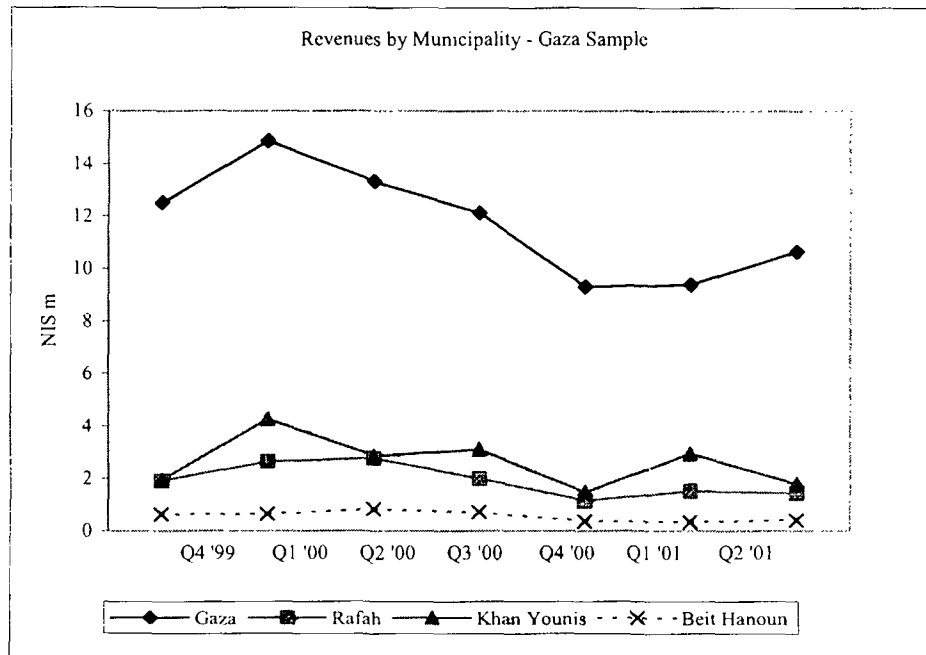
Net Revenues

Net revenues fluctuated considerably in the pre-*intifada* period and were already showing an increasingly negative trend (see figure A5.2 and table A5.6). Net revenues reached the lowest point in the first quarter of the *intifada*, at minus NIS 6 million. This deficit was brought under control in subsequent quarters (Q1 and Q2 2001) by a combination of increased revenue efforts and decreased spending. On average, the deficit has increased threefold since the beginning of the *intifada*, and the situation is even more serious when liabilities are factored in.

Table A5.5: Municipal Net Revenues in Period before and after the Start of the *Intifada* in October 2000, Gaza Sample (millions of NIS)

	<i>Q4</i>	<i>Q1</i>	<i>Q2</i>	<i>Q3</i>	<i>Period Average</i>
Pre- <i>intifada</i>	-3.2	4.1	-0.3	-3.6	-0.8
Post- <i>intifada</i>	-5.8	-0.9	-0.9	na	-2.5
Percentage change, pre- to post- <i>intifada</i>	-80	+70	+20	na	+340

Figure A5.3: Municipal Revenues, Expenditures, and Net Revenues Before and After the Intifada, Gaza Sample



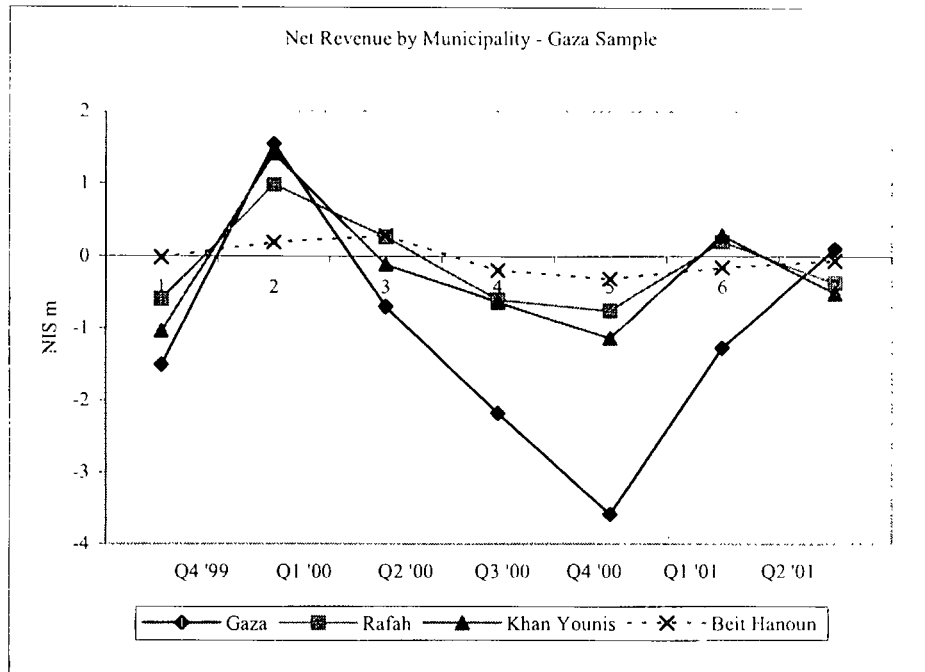
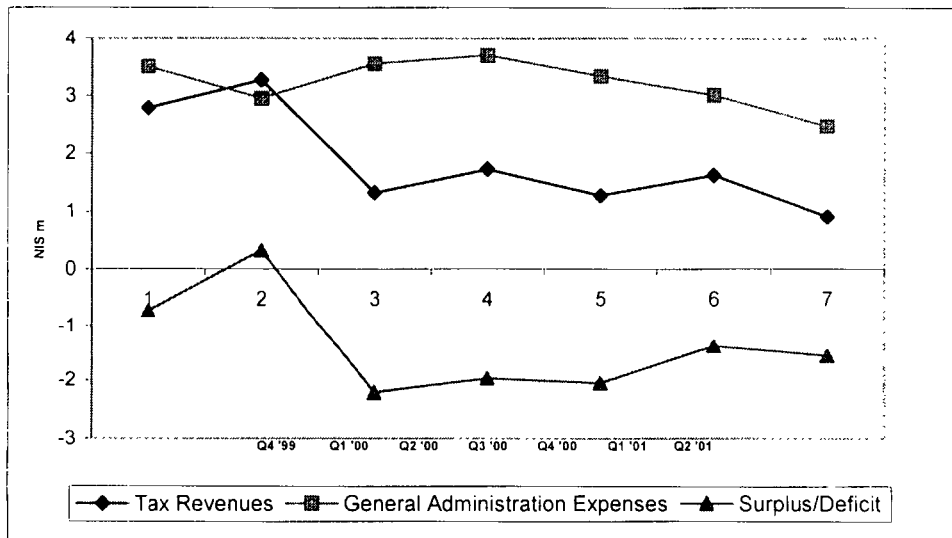
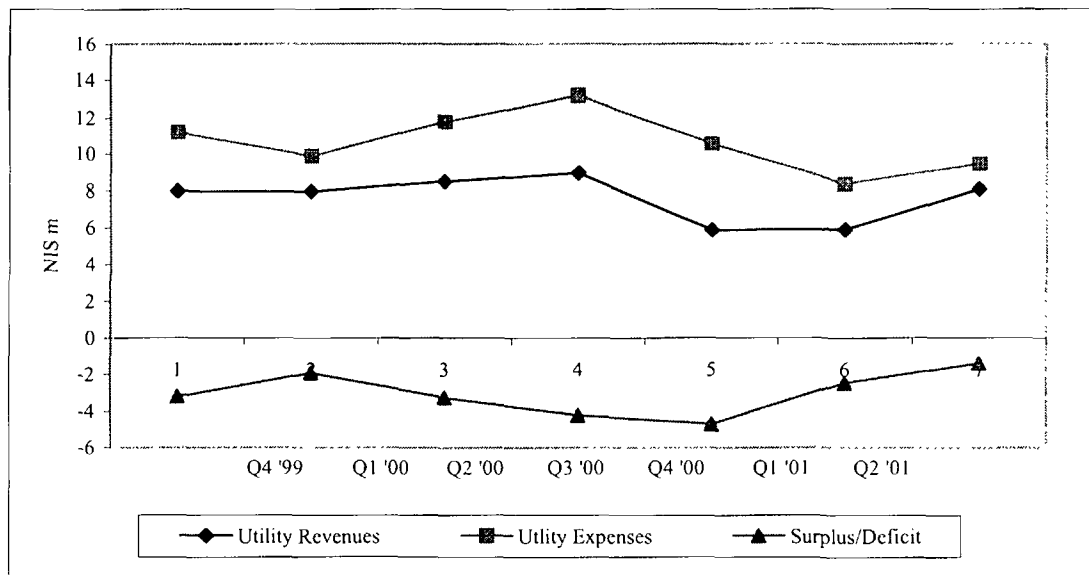
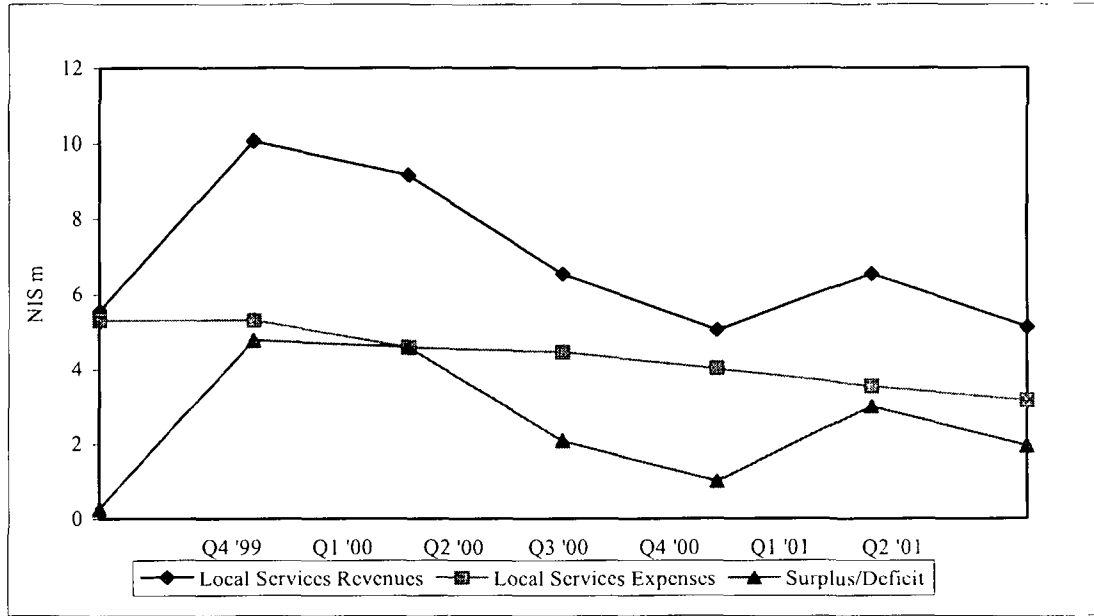


Figure A5. 4: Municipal Revenues and Expenditures before and after the Start of the *Intifada* in October 2000, by Category, Gaza Sample



Fifteen Months – Intifada, Closures and Palestinian Economic Crisis – An Assessment



ANNEX 6 THE EMERGENCY SERVICES SUPPORT PROGRAM

PROGRAM DESCRIPTION

The broad objective of the Emergency Services Support Program (ESSP) is to mitigate the deterioration of services brought about by the inability of central institutions and municipalities to meet their non-salary operating costs. The program will support recurrent budgetary expenditures through direct procurement of works, equipment, services, and supplies and through direct cash transfers. Limited to non-salary operating cost deficits, the ESSP will ensure that expenditures financed are accounted for within the overall fiscal framework of the Palestinian Authority.

In September 2001, President Arafat established an Inter-Ministerial Committee to work with the World Bank and other donors to identify budgetary needs for social service delivery ministries and municipalities. The needs were grouped by sector. The needs of the municipalities were defined in terms of specific services. Since the specific needs of municipalities differ, the distribution of funds between municipalities will take into account criteria to be established by the Ministry of Local Government, with donor assistance.

Support for the Operating Costs of Services Provided by the Palestinian Authority and Municipalities

Services to be supported are listed below.

Ministry of Health

- Medical expenses (drugs, medical disposables, laboratory and blood bank consumables).
- Utilities, fuel, and rental facilities.
- Contracts with local medical providers (NGOs and private hospitals).

Ministry of Education

- Textbooks.
- School furniture and equipment.
- School maintenance.
- Learning materials and lab equipment, reagents, etc.
- Teacher training programs for the new curriculum.

Ministry of Social Affairs

- Social welfare shelters.
- Training and rehabilitation centers.

Municipalities

- Solid waste management.
- Water and waste water management.
- Electricity generation, transmission, and distribution.
- Road maintenance.

Technical Assistance and Capacity Building to Service Delivery Ministries and Local Governments

While this is an emergency program, opportunities will be sought for providing capacity building inputs. The introduction of a management information system to improve the operation of social welfare programs by the Ministry of Social Affairs has been identified as one area requiring support. The project will provide additional technical assistance to ensure proper management by the implementation units which will be set up in the various ministries to manage the project.

Direct Cash Transfers

Since the primary aim of the ESSP is to bridge existing operating budget deficits and thereby sustain basic service delivery, it will also include items that cannot be procured but which have to be met through direct cash transfers. A large component of this program would be payments for the welfare recipients of the Ministry of Social Affairs. Today, some 45,000 families are registered with the social welfare program, but the ministry has been unable to make regular payments to this group during the *intifada*. This is a clear threat to the well-being of thousands of needy people, a majority of them women-headed households, the elderly, and the unemployed.

It is hoped that donors that do not have restrictions on making direct cash transfers to the Palestinian Authority's central budget will be able to finance this component of the program.

PROGRAM MANAGEMENT

The Ministry of Finance has overall coordination responsibility for ESSP, and will integrate the flow of funds into the overall expenditure management system. This will be ensured through careful review and monitoring of the disbursements of ESSP funds and consistent and timely information on planned and actual spending.

The Ministry of Finance has established a coordination unit, with a full-time project coordinator and other full-time staff to be hired as needed. The Ministry of Finance will also recruit an auditor for all project activities. Management of project sub-components will be handled by the budget units of the Ministries of Health, Education, Social Affairs and Local

Government. ESSP will provide technical support to these units to help with monitoring and compliance with World Bank procurement, financial management, and reporting procedures. Other donors providing financing for ESSP will work through this common management structure.

The Inter-Ministerial Committee, which includes representatives of the line ministries and the Ministry of Planning and International Cooperation, will provide overall monitoring through monthly reports to donors on expenditures made against program funds.

A committee of the Ministry of Finance and the social service delivery ministries will meet with participating donors every three months to exchange information on the budget and to coordinate efforts in support of Palestinian Authority operating cost and service delivery programs.

OVERALL COSTING OF THE PROGRAM AND EXISTING FINANCING GAP

The Palestinian Authority has proposed a program totaling US\$105 million, to cover budgetary needs for six months through June 2002. Of this amount, the Bank will provide an IDA credit for \$20 million, the European Commission will provide 20 million Euros, and up to seven EU member states will likely provide another 23 million Euros, for a total of about US\$38 million so far.

Following discussions with the Ministry of Finance and the Inter-Ministerial Committee, the allocation of Bank credit to various budgetary items has been agreed (see tables A6.1 and A6.2). To help ensure the availability of funds for all deficit items, the Bank has agreed to finance recurrent budget items such as utilities, fuel, and leases on the premise that payments would be made against receipts for services provided by contractors. The Bank will ensure that contracting for these services is in line with Bank procurement guidelines. Existing contracts will be reviewed to verify compliance with Bank procurement procedures, which require an open and competitive process.

Table A6.1 Allocation of Emergency Services Support Program Credits by Component (US\$ thousands)

<i>Sector and program component</i>	<i>Indicative cost^a</i>	<i>Bank financing^b</i>
<i>Ministry of Health</i>		
Medicines, other medical disposables, laboratory and blood bank consumables	13,800	5,800
Other operating expenses	8,901	1,650
Contracts with local providers (NGOs and private hospitals)	3,199	1,300
<i>Subtotal Ministry of Health</i>	<i>25,900</i>	<i>8,750</i>
<i>Ministry of Social Affairs</i>		
Social security net for hardship cases program	10,500	
Social shelters program	650	357
Rehabilitation and training centers program	850	415
Maintenance of shelters and training centers	525	525
<i>Subtotal Ministry of Social Affairs</i>	<i>12,000</i>	<i>1,297</i>
<i>Ministry of Education</i>		
Scientific textbooks	4,710	150
School furniture and equipment	1,200	1,200
Administrative expenses	1,850	1,800
School maintenance	0	0
Learning materials and labs	250	150
Teacher training programs for the new curriculum	90	0
<i>Subtotal Ministry of Education</i>	<i>8,100</i>	<i>3,300</i>
<i>Ministry of Local Government</i>		
Emergency support for solid waste sector	7,150	1,090
Emergency support for water and waste water sector	13,000	3,019
Emergency support for electricity sector	3,775	1,091
Emergency support for roads sector	15,000	0
<i>Subtotal Ministry of Local Government^c</i>	<i>38,925</i>	<i>5,200</i>
<i>Labor Union</i>		
Solidarity Fund	21,000	0
<i>Ministry of Finance and other ministries</i>		
Project Management and Capacity Building	1,000	600
<i>Unallocated</i>		<i>853</i>
Total financing required	105,000	20,000

a. These estimates cover a 6-month period running through June 2002.

b. The Bank Executive Directors approved a contribution of US\$20 million on IDA terms on 28 February 2002. This includes financing up to a total of US\$4 million for expenditures incurred before the date of Board approval.

c. The subcomponents pertaining to the municipalities also include non-budgetary items that represent expenditures that are related to the emergency and which are not accounted for as part of the regular municipal budgets.

ANNEX 7 PRIVATE SECTOR EMERGENCY RECOVERY FUND FOR WEST BANK AND GAZA

The private sector in the West Bank and Gaza continues to bear the brunt of the deteriorating economic situation. The private sector operates in a volatile environment of isolation, low demand, and increasing restrictions; physical damage to private sector assets is increasing, and entrepreneurs are struggling to survive. The longer the situation continues, the more difficult it will be for the private sector to recover once political stability is restored. With traditional sources of labor absorption (the public sector and jobs in Israel) essentially saturated, future sustainable employment and economic growth in the Palestinian economy will have to come from the private sector.

ESTIMATED DAMAGE TO THE PRIVATE SECTOR

By end-December 2001, nearly 60,000 private sector jobs in the West Bank and Gaza were lost, about 15 percent of the pre-crisis domestic private sector workforce.¹ The World Bank also estimates that physical damage to the private sector amounted to some US\$220 million by end-December 2001.² Losses from the private sector's contribution to GDP—a rough indicator of the economic losses to the private sector as a result of the crisis—are estimated at US\$1.05 billion for 2001 (table A7.1). The private sector's contribution to GDP has fallen from 88 percent to 69 percent of a considerably smaller economy in 2001.

Table A7.1: Estimated Private Sector Contribution to Projected GDP, Before and After the Start of the *Intifada* (US\$ million)

<i>Projections</i>	<i>1999</i>	<i>2000</i>	<i>2001</i>
Pre- <i>intifada</i> projections	3,341	3,526	3,784
Crisis-adjusted projections	3,341	3,080	2,734

Note: GDP measured at factor cost in constant 1998 dollars.

Source: World Bank staff estimates.

Employment figures also suggest that the burden of the crisis has not been equal across sectors, with some sectors (construction) hit harder than others (transport, commerce; see Table A7.2).

¹ Figure does not include employment lost in Israel, nor employment lost in East Jerusalem.

² Private buildings (residential, commercial) US\$45.2 million, Agriculture US\$176.6 million.

Table A7.2: Estimated Private Sector Employment, September 2000-December 2001

Sector	Number of jobs		Change (percent)
	September 2000	December 2001	
Agriculture and fishing	68,589	56,493	-18
Mining and manufacturing	73,569	59,902	-19
Construction	59,394	36,712	-38
Commerce	88,425	90,944	3
Transports and communication	28,289	27,568	-3
Other private services	60,032	49,441	-18
Total	378,298	321,060	-15

Note: Data exclude East Jerusalem.

Source: World Bank calculations based on data from the Palestinian Central Bureau of Statistics.

All areas of the private sector have been affected by the crisis. While more in-depth analysis is needed, this section briefly describes the impact in four sectors.

Tourism: The years 2000 and 2001 were expected to be record years for the tourism industry, but the outbreak of hostilities before the 2000 high season quashed those expectations and has led to a collapse in demand for tourism. Tourism sector income losses are estimated at some US\$400 million, with losses of more than 5,000 “direct” jobs.³ Nearly all tourism facilities are closed, and several hotels have incurred physical damage. In Bethlehem alone, the Paradise Hotel incurred damages of US\$3 million and the Jacir Palace damages of US\$1 million in October 2001. The Salomon Pools Hotel was also severely damaged by tank fire.

Prior to the *intifada*, entrepreneurs had invested heavily in developing new hotels and upgrading existing assets (hotels, parking, buses, stores) to accommodate the expected influx of tourists. This means that many entrepreneurs will be hard pressed to come up with the funds needed to meet reopening costs once the hostilities end. The new fleet of tourist buses has been reduced by nearly half, as many bus companies had to sell their buses at up to 25 percent discount because they could no longer afford the financing payments.

Manufacturing: Manufacturing businesses have reported an average 49 percent decrease in sales,⁴ a 26 percent increase in cost of inputs, and a 54 percent increase in transportation costs. In addition, all firms have reported losing markets because of the difficulty of moving finished goods and lower domestic demand. Many firms reported operating at less than 50 percent of production capacity (compared to 85 percent pre-crisis). In addition, wages to remaining workers were reduced by 28 percent.

Agriculture: The agriculture sector has been the hardest hit. As of December 2001, total estimated physical damage to the sector (to buildings, irrigation systems, wells, uprooted trees, and crops) was US\$176.6 million, of which Gaza’s share was US\$141.3 million.⁵

³ Including East Jerusalem.

⁴ Source: *State of Private Sector Survey*, August 2001, Center for Private Sector Development.

⁵ World Bank data.

Banking: The impact of the crisis on the banking sector, and on the quality of assets, is difficult to assess. Confidence in banks has remained high: consolidated customer deposits amounted to US\$3.11 billion⁶ as of October 2001, not much changed from the US\$3.12 billion as of October 2000. This is a positive sign. Consolidated credit facilities as of October 2001 were US\$836 million,⁷ down from US\$973 million as of October 2000—a substantial, yet understandable reduction in credit to the private sector. The quality of the assets has deteriorated, but the degree of deterioration is debatable. Estimates of non-performing loans vary from bank to bank but are believed to range between 10-20%.

The reaction of the commercial banks to the crisis has varied. Many have rescheduled non-performing loans, increased loan loss provisioning⁸ and cash reserves, and emphasized collection while tightening the issuance of new credit (for example, some banks now require up to 70 percent cash collateral). Once hostilities cease, stabilizing the banking sector will be a top priority.

THE PROPOSED PRIVATE SECTOR EMERGENCY RECOVERY FUND

Objectives and Structure

Despite the difficult business climate, Palestinian entrepreneurs have shown considerable resilience. Many businesses have adapted to the current environment and have scaled back to sustainable levels, or have identified new opportunities (the stone and marble industry, for example, has managed to penetrate new markets, with export sales reaching US\$90 million in 2001, up from US\$17.6 million in 1998; some manufacturers have coped with internal closures by increasing their levels of raw material inventory to avoid shut-downs, and by establishing new distribution networks/centers). However, after more than 18 months of violence, most entrepreneurs' resources have been stretched to their limits, and a number of investors have suffered physical damage.

Since a functioning private sector is crucial for the survival of the Palestinian economy, the World Bank Group proposes the establishment of a donor-financed emergency support fund. An initial proposal was discussed with donors in January 2002. The consensus was that such a fund should provide some support during the crisis and that donors should not await a return to more normal times before establishing it. The fund should therefore aim to provide assistance to enterprises that are potentially viable/able to continue operations during the crisis, but which lack access to financial and technical resources; it should also provide for some physical reconstruction. The fund's main emphasis, however, would be on restarting private sector operations once the crisis is over and market demand picks up again. Since most larger Palestinian businesses would be able to obtain financial support independently, it is anticipated that the fund would target small and medium-size enterprises, which account for some 90 percent of businesses.

⁶ Excludes deposits of the Palestinian Authority, public institutions, and local authorities of US\$231 million.

⁷ Amount excludes credit facilities equal to US\$339 million granted to the PA, and US\$62 million granted to public institutions and local authorities.

⁸ All banks are required to follow Palestine Monetary Authority (PMA) loan loss provision guidelines which were relaxed during the crisis. The PMA allows banks to deduct certain types of collateral.

The fund might work best as a partnership of local businesses and the donor community.

Such a fund might

- **Rehabilitate physical damage**, using intermediaries to provide part of the funds necessary to repair or replace private sector business property (including buildings, equipment, and inventory) damaged by the crisis and not covered by insurance because of war/civil strife exclusion clauses. Claims could be verified by pre-selected insurance companies to determine the extent of damage and verify the costs to repair or replace the assets. Appropriate safeguards would be developed to minimize moral hazard and ensure thorough supervision of funding operations.
- **Provide working capital loans** through intermediaries, to assist businesses that have incurred substantial economic injury to continue operations during the crisis, and/or to restart operations once demand picks up again. The fund could help businesses make payments on short-term notes and accounts payable, to continue to meet long term loan payments, and to maintain reasonable working capital positions. The fund could provide partial guarantees/first-loss coverage, share loan risk with pre-selected financial intermediaries on a *pari-passu* basis (agency lines), or simply provide credit lines to the intermediaries. Loan durations should be tailored to each borrower's financial capabilities, and could range up to 7 years. Restrictive collateral requirements could be relaxed to allow businesses to secure loans with assets such as receivables from the PA. Efforts could be made to facilitate export credits where feasible. Re-flows on account of fund loans could be used to finance other fund activities, such as technical assistance. The loans would be supervised by the intermediaries.
- **Assist commercial banks to restructure their balance sheets**, by purchasing non-performing loans or providing tier-2 capital in the form of subordinated loans. Most commercial banks have rescheduled loans to keep their portfolios cosmetically healthy, but indications are that the portfolios have suffered from the crisis, and that such measures are no lasting solution. By purchasing non-performing loans, the fund would help banks to resume regular lending more rapidly. Only loans that have become non-performing because of the crisis would qualify in this instance.
- **Provide technical assistance** to Palestinian businesses to help them adjust to the crisis, or get back on their feet during or after the crisis. Technical assistance could be made available through vouchers that can be used to procure consulting services from selected intermediaries. Services could cover restructuring and business plan preparation. Technical assistance is possible under the current conditions, and existing providers have successfully adapted their services to the current environment.⁹

Size of the Fund, Financing

The amount needed to support the Palestinian private sector during and after the crisis is difficult to establish. While the appropriate size of such a fund would be discussed with other

⁹ One such provider has reported impressive achievements that include a 10 percent-plus increase in capacity utilization and an operation efficiency of more than 70 percent among assisted firms.

donors, it has been tentatively sized at US\$40 million for in-crisis activities, with a further US\$100 million to follow in the post-crisis phase.

It is unlikely that any private sector entity could contribute to the fund. The Palestinian private sector has been severely hurt by the crisis and will probably be unable to assist with reconstruction efforts. The international private sector has shown no particular interest in assisting at this point in time.

Fund Structure and Administration

An advisory board including donor representatives could oversee administration of the fund. Members of the Palestinian diaspora have indicated strong support for the fund's objectives and could be asked to serve on the advisory board. One advantage of donor participation would be to encourage donor representatives to remain engaged on the needs of the private sector. The board could consider requests for additional types of support that fall outside the fund's starting mandate, thereby giving the fund flexibility to develop in accordance with emerging needs.

It is proposed that the fund act only through intermediaries, as a wholesale operation. The fund's governance structure would thus limit its involvement to selecting and supervising the chosen intermediaries, which would in turn be responsible for specific investment and technical assistance decisions. This would require the establishment of clear eligibility criteria and safeguards.

Based on this wholesale approach, the fund could be managed by IFC using seconded IFC staff, or by donors. Alternatively, the fund could be managed by a professional management company, selected through competitive bidding. Donor views will be sought on the best route to follow. The fund could be headquartered in the West Bank.

Next Steps

The World Bank will present this proposal to the Ad Hoc Liaison Committee to ascertain donor support for the fund.

Provided there is donor interest and donor commitment in principle to financing the fund, the World Bank and IFC would undertake in-depth appraisal work, including a review of potential intermediaries and detailed fund structure and operating modalities. The Bank could also consider making a financial contribution if sufficient donor interest is apparent.

