

# Implementing the Palestinian Reform and Development Agenda

Economic Monitoring Report  
to the Ad Hoc Liaison Committee

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## Acronyms

AHLC	Ad-Hoc Liaison Committee
AMA	Agreement on Movement and Access
COGAT	Coordinator of Government Activities in the Palestinian Territories
CTA	Central Treasury Account
EC	European Commission
EU	European Union
GDP	gross domestic product
GNP	gross national product
GOI	Government of Israel
ICA	Investment Climate Assessment
IMF	International Monetary Fund
LACS	Local Aid Coordination Secretariat
MENA	Middle East and North Africa
MOF	Ministry of Finance
MOP	Ministry of Planning
MTEF	Medium-Term Expenditure Framework
NGO	non-governmental organization
OCHA	UN Office for the Coordination of Humanitarian Affairs
PA	Palestinian National Authority
PCBS	Palestinian Central Bureau of Statistics
PRDP	Palestinian Reform and Development Plan
PWA	Palestinian Water Authority
QR	Quartet Representative
SWG	Sector Working Group
TA	technical assistance
UNRWA	United Nations Relief and Works Agency
UNSCO	Office of the United Nations Special Coordinator
WBG	West Bank and Gaza

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## Executive Summary

***At the Ad Hoc Liaison Committee (AHLC) Meeting in New York on September 23rd, 2007, the World Bank summarized the changing course of the Palestinian economy since 2000*** from one driven by investment and private sector productivity to one sustained by government spending and donor aid. After a good performance in the latter 1990s, the fragile Palestinian economy entered a gradual downward cycle of crisis and dependence, as it was confounded by political and security events in the West Bank and Gaza (WB&G), the continued growth in settlements, Israeli restrictions on movement and access since the Second Intifadah, and finally the 2006 drop in donor aid. Unable to find opportunities in a shrinking private sector, a young and rapidly-expanding labor force has turned to the public sector to create jobs and increase spending to alleviate poverty, at the expense of further investment in the economy's productive potential. This trend, underway since 2000, was most acute in the aftermath of the elections in 2006.

***The analysis that was presented at the 2007 AHLC showed that reversing this downward trend required parallel actions by the Palestinian Authority (PA), Israel and the donors. In addition, these parallel actions were regarded as effective insofar as they addressed the entirety of the Palestinian population.*** Reform and development of the Palestinian economy – including Gaza, which represents about 40% of the population – and its institutions were to resume through the implementation of the PA's Palestinian Reform and Development Plan (PRDP). To succeed, the PRDP was to be underwritten by donors and supported by Israeli efforts to loosen restrictions on the movement of goods and people within and out of the WB&G. It was argued that the impact of donor aid is highest when accompanied by concrete and parallel PA and Israeli actions, but that the consistent flow of aid should not be predicated on them – aid remains critical to ensure the survival of Palestinian institutions that underpin the peace process.

***The expectations set at the AHLC in New York were that several developments could trigger a change in the course of the Palestinian economy:*** not least the Annapolis conference of November 27, 2007, where Prime Minister Olmert and President Abbas agreed to resume peace negotiations and resolve core issues by the end of 2008; the progress in bilateral discussions on key issues and the formation of seven Israeli-Palestinian working groups; and the Paris Donor Conference on December 17, 2007, where representatives of 87 states and organizations pledged US\$7.7 billion in financial support to the PRDP for 2008-10. In furtherance of these efforts, several critical measures were initiated by the parties, including those by Quartet Representative Tony Blair, to rebuild confidence and momentum towards an economic recovery.

***This report will show that – despite these and other efforts since the 2007 AHLC – the virtuous cycle of economic growth arising from parallel actions by the PA, Israel and the donors has not been fully realized.*** The formation of the Caretaker Government in mid-2007, and the resumption of aid have reversed the impacts of the aid boycott in 2006 and 2007, but only partially. Real GDP was negative in the first half of 2007 but began to recover in the West bank during the second half. Because of the situation in Gaza, real GDP growth in 2007 is estimated to be about 0%, which given the rapidly growing population indicates falling per capita income. The contributing effects of the closures and movement restrictions cannot be overestimated.

***Moreover, economic indicators have not changed considerably, despite the resumption in aid.*** Unemployment in WB&G stood at nearly 23% in 2007, up from only 10% before the beginning of the Intifadah in 2000. Unemployment is highest in Gaza, at nearly 33% of the active work force. This rate is likely to become much higher as the layoffs in the industrial sector become permanent.

***As a tripartite action plan, the implementation of the PRDP has begun in earnest, but progress has been only partial.*** The PA has implemented a sequence of steps centering on control of expenditures and medium-term reforms to bring the PA back to financial sustainability, and has achieved some important milestones in this area. The PRDP has been underwritten by donors who, at the time of this report, had already transferred half of their pledges made in Paris towards recurrent expenditures, either through direct transfers to the PA's Central Treasury Account, through the EC's new PEGASE instrument, or through the World Bank's new PRDP-linked Multi-Donor Trust Fund. The efforts of the Quartet Representative have also introduced a set of concrete deliverables that, if adopted by the parties, could help trigger a much-needed private sector response. However, the private sector revival required for a virtuous cycle of growth has not been realized due to continued restrictions on movement and access. As a result, the economic scenarios presented at the Paris Conference, proposing that the implementation of Palestinian commitments alone is a necessary but insufficient condition for economic growth, have been confirmed by the zero GDP growth in the WB&G in 2007. As for 2008, the IMF analysis and AHLC Report note a projected GDP growth of 3.0% that, taking into account population growth, leaves per capita incomes static if not lower than the previous year.

***Regardless of the scenario, PA reforms and adequate donor aid – covering both recurrent and development spending – remain necessary but insufficient preconditions for economic recovery in the WB&G.*** A scenario where PRDP reforms continue, where they are fully funded by donors, and where private sector growth and trade is revived as a result of easing movement and access restrictions, will result in accelerated growth rates at double digit levels. Embedded in this scenario is a recovery in Gaza driven by the resolution of the current stalemate, and its immediate inclusion in the benefits of reforms, donor aid, and the lifting of movement restrictions.

# I. Introduction

1. *At the Ad Hoc Liaison Committee (AHLC) Meeting in New York on September 23<sup>rd</sup>, 2007, the World Bank summarized the changing course of the Palestinian economy since 2000* from one driven by investment and private sector productivity to one sustained by government spending and donor aid. During this period, per capita GDP in 2007 fell to 60% of its levels in 1999. After a good performance in the latter 1990s, the fragile Palestinian economy entered a gradual downward cycle of crisis and dependence, as it was confounded by political and security events in the West Bank and Gaza (WB&G), the continued growth in settlements, Israeli restrictions on movement and access since the Second Intifadah, and finally the 2006 halt in donor aid<sup>1</sup>. Unable to find opportunities in a shrinking private sector, a young and rapidly-expanding labor force has turned to the public sector to create jobs and increase spending to alleviate poverty, at the expense of further investment in the economy's productive potential. This trend, underway since 2000, was most acute in the aftermath of the elections in 2006.
2. *The analysis that was presented at the 2007 AHLC showed that reversing this downward trend required parallel actions by the Palestinian Authority (PA), Israel and the donors. In addition, these parallel actions were regarded as effective insofar as they addressed the entirety of the Palestinian population.* Reform and development of the Palestinian economy – including Gaza, which represents about 40% of the population – and its institutions were to resume through the implementation of the PA's Palestinian Reform and Development Plan (PRDP). To succeed, the PRDP was to be underwritten by donors and supported by Israeli efforts to loosen restrictions on the movement of goods and people within and out of the WB&G. It was argued that the impact of donor aid is highest when accompanied by concrete and parallel PA and Israeli actions, but that the consistent flow of aid should not be predicated on them – aid remains critical to ensure the survival of Palestinian institutions that underpin the peace process.
3. *The expectations set at the AHLC in New York were that several developments could trigger a change in the course of the Palestinian economy:* not least the Annapolis conference of November 27, 2007, where Prime Minister Olmert and President Abbas agreed to resume peace negotiations and resolve core issues by the end of 2008; the progress in bilateral discussions on key issues and the formation of seven Israeli-Palestinian working groups; and the Paris Donor Conference on December 17, 2007, where representatives of 87 states and organizations pledged US\$7.7 billion in financial support to the PRDP for 2008-10. In furtherance of these efforts, several measures were initiated by the parties, and supported by Quartet Representative Tony Blair, to rebuild confidence and momentum. These include, among others, steps to unshackle critical donor projects in the WB&G, removal of a number of physical impediments to movement in the West Bank, deployment of 300 PA security forces in Nablus in a bid to impose law and order, and the introduction of several Quick Impact Projects to create jobs and other economic impacts on the ground.
4. *The PA has also achieved early progress in the implementation of the PRDP.* The PA's Plan, comprising a sequence of steps centering on control of expenditures and medium-term reforms to bring the PA back to financial sustainability, has also achieved some important milestones. This has been underwritten by donors who, at the time of this report, had

1 In response to this statement, the Israeli Authorities stress "the legitimate security concerns that necessitate these restrictions." The Authorities also note that the decline in the Palestinian economy is also due to the Hamas takeover of Gaza.

already transferred half of their pledges made in Paris towards recurrent expenditures, either through direct transfers to the PA's Central Treasury Account, through the EC's new PEGASE instrument, or through the World Bank's new PRDP-linked Multi-Donor Trust Fund.

5. ***However, as this report will show, the virtuous cycle of economic growth arising from parallel actions by the PA, Israel and the donors has not been realized.*** Despite reforms by the PA, the implementation of the PRDP- fundamentally a tripartite effort- remains relevant yet incomplete. As a result, the IMF estimates zero total real GDP growth in 2007, and projected GDP growth of 3.0% that, taking into account population growth, leaves per capita incomes static if not lower than the previous year.

6. ***Embedded in the PRDP are assumptions on the growth of the economy, the revival of the private sector, and the PA's ability to achieve a predictable financing horizon.*** These assumptions are linked to progress on movement and access, and on steps by the donors to quickly translate their pledges to transfers, particularly towards the PA's recurrent budget. Progress has been varied on these fronts, as the PA continues to receive recurrent budget support on an ad hoc basis, and is unable to reap the benefits of a revitalized private sector due to remaining movement restrictions. Furthermore, raids by the Israeli Defence Forces (IDF) into parts of the WB&G continue.<sup>2</sup> Israeli settlement activity continues in the West Bank including the issuing of tenders for new construction<sup>3</sup>. According to the UN, obstacles to movement within the West Bank remain significantly higher than in 2005. Two-thirds of the 723.3 km Separation Barrier between Israel

and the West Bank is now complete, with 12% of the area of the West Bank isolated in enclaves and West of the Barrier. Violence continues: scores of Palestinians have been killed, injured or detained by the IDF, and numerous civilians within Israel have been killed and injured by over 3,500 rockets fired by Palestinian militants in Gaza since Israel's disengagement in late 2005<sup>4</sup>. On February 4, 2008, the first suicide bombing in a year took place in the southern Israeli town of Dimona, followed by a shooting attack on a Jewish Seminary in Jerusalem on March 6<sup>th</sup>. Lastly, Gaza's population remains isolated and supplies remain confined to humanitarian items. Fuel supplies to the Strip have been repeatedly restricted, most recently as a result of an attack on Israeli civilians in nearby Nahal Oz on April 9<sup>th</sup>.<sup>5,6</sup>

2 In response to this statement, the Israeli authorities note that such incursions are necessary to safeguard against continued attacks against Israeli civilians. Moreover, efforts underway to facilitate the mobilization of roughly 700 PA security personnel into Jenin reflect the desire of the Israeli authorities to empower PA security to undertake such mitigation in the future.

3 For example, on December 4th tenders were announced for 307 new housing units in the Israeli settlement of Har Homa in the West Bank, representing about half of the total 747 housing units tendered after Annapolis. Israel Lands Administration (ILA) and Ministry of Construction & Housing (MoCH).

4 Figure obtained from Israeli COGAT.

5 At the time of this report, fuel supplies to the Gaza Power Plant have been resumed. However, fuel for other purposes continues to be restricted.

6 At the time of this report, a suicide attack on the Kerem Shalom Crossing between Israel and Gaza took place on April 19th, injuring several Israeli soldiers.



## II. Economic Developments and Prospects

7. ***Beyond the impacts of the protracted economic downturn since restrictions were imposed after the Second Intifadah, the Palestinian economy faces a more hazardous prospect-*** a fundamental change in its composition, with GDP increasingly driven by government spending and donor aid, leaving little resources for investment thus further reducing the productive base for a self-sustaining economy. Contributing to the crisis is an expanding labor force and a shrinking private sector, placing further pressure on the public sector to become the primary alternative for jobs.
8. ***During the fiscal crisis in 2006 and 2007, the Palestinian economy relied on borrowing, remittances and increased aid outside the standard PA channels to sustain both public and private consumption. Investment, however, fell sharply.*** According to the Palestinian Central Bureau of Statistics (PCBS), household consumption dropped by only 0.6% between 2005 and 2006. However, investment fell to precariously low levels. Public investment in the last two years has nearly ceased as almost all government funds have been used to pay salaries and cover operating costs. The IMF estimates that private investments fell by over 15% between 2005 and 2006 and there is no evidence that it significantly increased in 2007. Gross capital formation by the private sector remains less than 16% in 2007.<sup>7</sup>
9. ***The formation of the Caretaker Government in mid-2007, and the resumption of aid have reversed the impacts of the aid boycott in 2006 and 2007, but only partially.*** Real GDP was negative in the first half of 2007 but began to recover in the West bank during the second half. Because of the situation in Gaza, real GDP growth in 2007 is estimated to be about 0%<sup>8</sup>, which given the rapidly growing population indicates falling per capita income<sup>9</sup>. Overall per capital income is estimated to be nearly 40% less than its peak in 1999. The contributing effects of the closures and movement restrictions cannot be overestimated. Between 1995 and 2000, the Palestinian economy was growing at an average rate of 6% per year. If that trend had continued after 2000, when restrictions intensified, real GDP may have been more than double its current value at over \$8 billion.
10. ***Moreover, economic indicators have not changed considerably, despite the resumption in aid. Unemployment in WB&G stood at nearly 23% in 2007, up from only 10% before the beginning of the Intifadah in 2000.***<sup>10</sup> Unemployment is highest in Gaza, at nearly 33% of the active work force. This rate is likely to become much higher as the layoffs in the industrial sector become permanent. The unemployment rate in the West Bank is approximately 19%. The percentage of Gazans who live in deep poverty<sup>11</sup> has been steadily increasing, rising from 21.6% in 1998 to nearly 35% in 2006. With the continued economic decline in 2007 and the implementation of even stricter closures on Gaza, the current deep poverty rate is expected to be higher than 2006 levels. These poverty levels reflect actual consumption. If remittances and food aid are excluded and poverty is based only on household income, the poverty rate in Gaza jumps to almost 67%. The increase in poverty in the West Bank is lower, but is still significant.

7 IMF Report to the AHLC, May, 2008.

8 IMF Report to the AHLC, May 2008. PCBS quarterly statistics suggest that total growth may be slightly higher. However, taking into account population growth rates would lead to the same conclusion regarding the low-to-negative per capita growth rates.

9 At the time of this report, no breakdown in this zero GDP growth figure between West Bank and Gaza was available. In view of the collapse in Gaza's economy since June 2007, it is clear that GDP in the West Bank must have been positive. However, given that the population in the West Bank is almost double that of Gaza, it can be inferred that modest GDP growth in the former was not sufficient to offset the severe contraction in GDP in the latter.

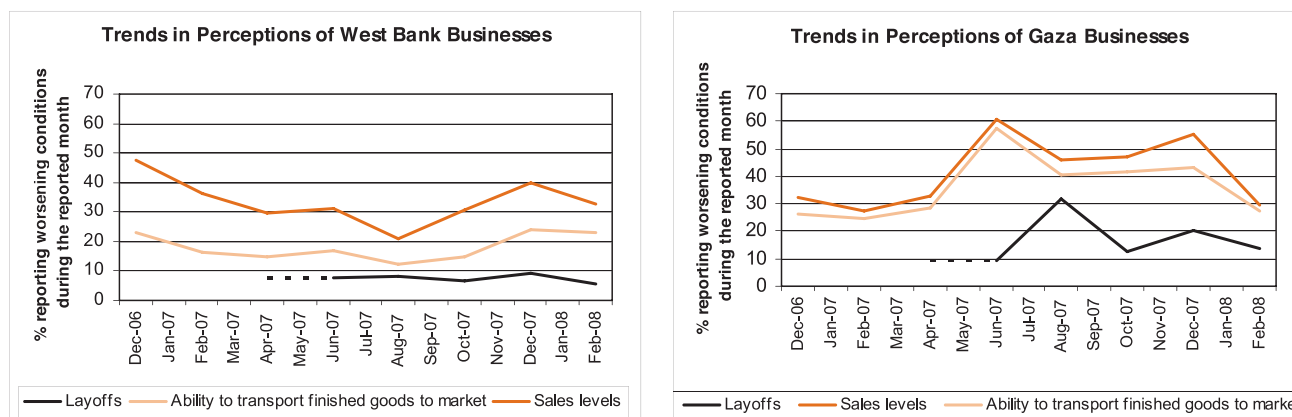
10 PCBS Labor Force Studies, 2008.

11 Defined as a NIS 1,837, budget for a family of six for food, clothing and housing only.

11. **Overall, a large proportion of the private sector in both the West Bank and Gaza continue to report worsening conditions in their operations.** In Gaza, the number of businesses reporting worsening conditions in terms of sales, ability to transport goods to markets, and number of layoffs peaked in June 2007 – August 2007 when the imposition of

near complete closure of Gaza began. In the West Bank, the percent of businesses reporting increasingly worse conditions actually rose in the 4<sup>th</sup> quarter of 2007 with 24% reporting increasing difficulties in transporting goods, 40% reporting falling sales, and 9% reporting layoffs in December 2007 (see Figure 1).<sup>12</sup>

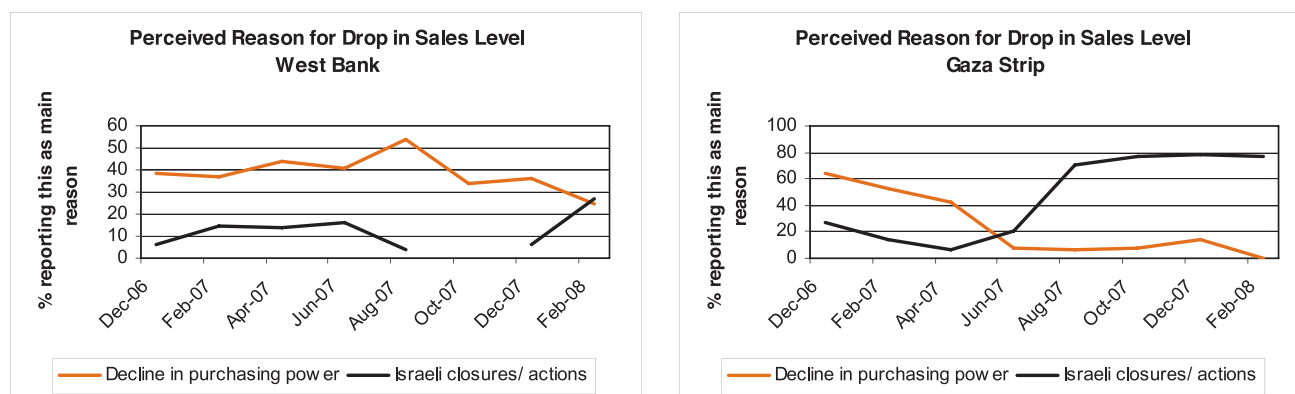
**Figure 1: Private Sector Perceptions**



12. **Private sector activity remains constrained and hampered by movement and access restrictions and reduced consumption due to lower purchasing power.** In the West Bank, business owners perceive lower purchasing power due to the economic downturn on the one hand and Israeli closures, restrictions, and military actions on the other as nearly equal

contributors to depressed sales (at about 25% of respondents). Unsurprisingly, in the Gaza Strip the vast majority of businesses attribute their depressed sales primarily to Israeli closures, up from about 14% one year ago when the West Bank businesses responded with the same percentage (see Figure 2).

**Figure 2: Private Sector Perceptions on Drops in Sales**



<sup>12</sup> Survey on the Perceptions of the Owners/Managers of Industrial Establishments Regarding the Economic Situation, PCBS, various months from 2006 – 2008. Based on a survey of 350 - 500 establishments in the West Bank and Gaza.

13. ***The government's 2008 budget, approved on March 31<sup>st</sup>, envisions total spending of \$3.338 billion and a financing gap of over US\$2 billion that must be filled by external aid. This is in sharp contrast with the surplus budgets that prevailed in 1999 when the economy was growing.*** The PA has announced a Palestinian Reform and Development Plan (PRDP) to increase revenues reduce expenditures and introduce sector reforms to enhance efficiency. But even with these measures and assuming resumed economic growth, the fiscal gap for recurrent expenditures alone is projected to remain high, at around \$1.63 billion in 2008.

14. The current status of the economy is a result of the need for concrete PA reforms, matched with an immediate resolution of the movement and access restrictions related to Israeli security concerns and settlement growth which have fragmented the economy into disconnected cantons. While the PA has moved ahead with its economic reforms, albeit slowly, there has been little progress on relaxing movement and access constraints. In the West Bank, the number of checkpoints increased from 376 in August 2005 to 580 in early 2008. There are currently 149 settlements in the West Bank, including East Jerusalem, and roughly 110 outposts many of which are regarded as illegal by the Israeli Government. Since the 1993 Oslo Accords, the Settlement population has risen % to approximately 40,000. Some 38% of the West Bank has been confiscated for current or future settlements, outposts, closed military areas, municipal boundaries and settlement regional jurisdiction. Palestinians without special permits are restricted from important agricultural areas in the Jordan valley and producers are cut off from the East Jerusalem market. The GoI has established five crossing points to transfer commercial goods between Israel and the West Bank. The crossing points use a back-to-back cargo transfer system similar

to the one for crossing into Gaza, however the system is unlikely to accommodate the expected volume of traffic. Over 95% of Palestinian trade is with Israel.

## Update on the Gaza Strip

15. ***The continued closure policy on Gaza since the events of June 14<sup>th</sup>, 2007 has considerably eroded whatever private sector backbone remained in the economy, and in a manner that is progressively more difficult to reverse.***<sup>13</sup>

As mentioned earlier, the percentage of Gazans who live in deep poverty has risen to nearly 35% in 2006, and is expected to have increased further in 2007 and 2008. If revised to exclude remittances and food aid, this poverty rate is closer to 67%.

16. Over 53%<sup>14</sup> of employment in Gaza is private sector-driven, representing more than 100,000 jobs. Recent data on Gaza's GDP are not readily available, but Gaza contributed \$1.3 billion to Palestinian GDP in 2003 (44%), of which the private sector is the main economic driver. The impacts of the closures will become less reversible with time. Most Gazan industries are export-oriented and have purchase and supply contracts with Israeli and other firms. Gazan manufacturers rely almost entirely on imports for their inputs and until recently, about 76% of their furniture products, 90% of their garments and 20% of their food products were exported to Israel, and some to the West Bank.

17. ***According to business associations in Gaza, the current restrictions have led to the suspension of 96% of Gaza's industrial operations,*** including domestic and export-oriented manufacturing and agriculture, and services (see Table 1). They could access neither the inputs for production nor any export markets, transforming Gaza into a consumer economy driven primarily by public

13 In response to this statement, the Israeli authorities note the need to stress the reasons behind the current closure policy, including the takeover of Gaza by Hamas militants, and the continued attacks on Israeli civilians. According to Israeli COGAT, about 3,500 homemade rockets have been launched from Gaza into Israel. In March alone, an estimated 110 rockets have been launched into Israel.

14 Q4 2007 as reported by PCBS Labor Force Press release, March 2008.

sector salaries and humanitarian assistance. During 2007, the furniture and garment sectors lost potential export sales of approximately \$17 million and \$24 million, respectively. In June 2007, about 6,500 worked in the furniture sector, and 25,000 in the garment sector. As of January 2008, these numbers dropped to 75 and zero, respectively. According to the Palestinian Contractors Union, the number of construction establishments dropped from 120 in January 2007 to almost zero in January 2008.

All the construction and development projects, including those for UNDP and UNRWA which are valued at more than \$116 million, have been halted to the absence of construction materials. As a result of the closure imposed on Gaza since June 2007, the halted construction projects are estimated at \$240 million and 42,000 workers were laid off.<sup>15</sup> The scarcity of construction materials has resulted in a considerable rise in construction materials cost<sup>16</sup>.

**Table 1: Industrial Decline in Gaza<sup>17</sup>**

	June 2005	July 2007	December 2007	January 2008	February 2008	March 2008
Working Establishments	3,900	780	195	150	150	130
Working Employees	35,000	4,200	1,750	1,500	1,500	1,300
Note: PCBS data shows a less dramatic decrease in industrial employment, from 17,000 in Q2 of 2007 (April-June) to 11,000 in Q3 of 2007 (October-December), a drop of 33%. PCBS uses ILO standards in the determination of employment.						

18. ***The agriculture export sector, with more than 40,000 workers, has been particularly affected*** as it is entirely dependent on the export market and on the imports of fertilizers, pesticides, packaging materials, and other inputs. To illustrate, as a result of border crossings closure, Gaza's carnation farmers were able to export 10 million flowers out of at least 45 million flowers which resulted in \$6.5 million loss, and thus resorted to selling flowers as animal feed. It is worth mentioning that carnations and strawberries are the two largest agricultural exports from Gaza. Both carnations and strawberries can generate up to \$20 million in income (\$10 million each). The estimated lost income from strawberry sales during 2007/2008 season is approximately \$7 million.<sup>18</sup>

19. ***The reduction in fuel imports into Gaza has impacted both private sector activities and donor projects.*** The Israeli policy of reduction of fuel supplies as a response to continued attacks on Israel began on October 28<sup>th</sup>, 2007. Between January and September 2007, approximately 18 million liters of fuel were imported per month. This dropped by about 25% in November 2007, 14% in December, 20% in January 2008, 38% in February, and 25% in March. In February 2008, gasoline (diesel) dropped by approximately 67% and benzene steeply dropped by about 80%.<sup>19</sup>

15 According to PCBS, employment in the construction sector dropped by 78% between Q2 and Q4 of 2008.

16 According to the Gaza Business Associations, the closures on Gaza have led to accumulated losses of \$500 million. In addition, the banking sector has dropped by 60%.

17 Original data from Industrial associations in Gaza reported to Paltrade and recent World Bank interviews with Palestinian Federation of Industries (PFI).

18 As reported by Gaza Agricultural Associations and Paltrade. PCBS data differs, showing an increase in

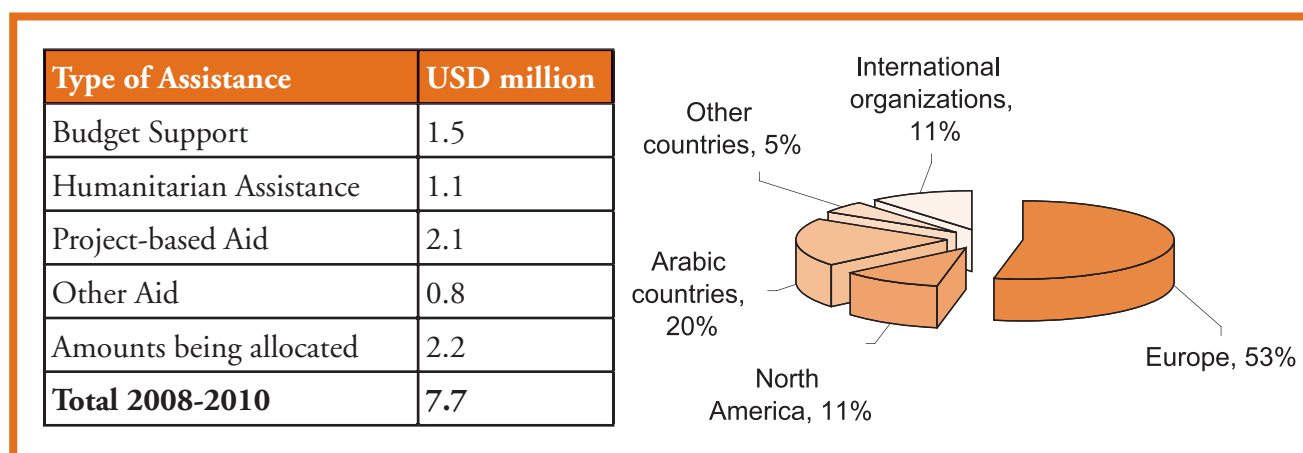
19 Paltrade, Gaza Terminals Movement Monitoring, Semi-annual Report (Oct 2007 - Mar 2008) April 7, 2008.

## III. The Palestinian Reform and Development Agenda

### III.A The Palestinian Reform and Development Plan (PRDP)

20. *Presented at the Paris Donor Conference, the PA's PRDP for 2008-10 represents both a Palestinian-owned plan for assigning resources to reform and other priorities, and a tripartite action plan for rehabilitating the Palestinian economy.* It seeks to stabilize the PA's fiscal situation by containing recurrent spending and, as the economy improves, shifting resources towards development spending. In the medium-term, the PA plans to reduce the budget deficit from about 28% of GDP in 2007 to 17% in 2010. This assumes PA implementation of a fiscal containment program, donor assistance for the PA's recurrent expenditures and public investment program, and a revival of the private sector resulting from Israeli removal of restrictions on movement and trade.
21. *International support for the PRDP has been quite strong, with total pledges at Paris of over \$7.7 billion<sup>20</sup>.* As of the time of this report, approximately \$600 million in recurrent budget support alone was transferred to the PA, and dialogue between the donors and the PA, through the local aid coordination groups, was underway to agree on priorities for development projects (see Figure 3).

Figure 3: Outcome of the Paris Pledging Conference, December 17<sup>th</sup>, 2007



22. *The PA has already taken concrete steps to implement the PRDP.* Key reforms have been undertaken to control the largest spending categories, including the public sector wage bill and net lending. Initial progress has also been made to articulate a three-year development plan that reflects detailed discussions within the PA ministries. These initiatives build on early steps by the PA in mid-2007 to rehabilitate parts of the Public Financial Management system, and reconsolidate the Central Treasury Account (CTA), among others.
23. *As part of a collective effort to jump-start the economy, a set of Quick-Impact Projects have also been identified by Quartet Representative Blair, Palestinian Prime Minister Fayyad and Israeli Defense Minister Barak.* These projects, embedded in the PRDP, are intended to provide quick wins, create employment and encourage additional private investment. Equally importantly, they are intended to showcase the dividends of collective action by the Palestinian and Israeli authorities in promoting private sector development in the Palestinian territories.

20 This figure is in excess of the \$5.6 billion gap presented in the PRDP for the 3-year period.



The projects identified cover a wide array of sectors, including tourism, education, housing, industrial estates, agriculture, and water and sanitation. In addition to this, the PA through the Prime Minister's Office has launched 300 small infrastructure projects focusing on rural areas.<sup>21</sup>

24. ***Ultimately, and as discussed below, the PRDP will need parallel actions by three parties in order to result into economic growth***, including fiscal and other reforms by the PA, as well as

law and order; sufficient donor funding for PA operations and development programs; and significant easing, with a view to eliminating movement and access restrictions. World Bank and IMF analysis<sup>22</sup> presented in Paris suggested that PA reforms, while critical, alone will not achieve the modest growth anticipated by the PRDP. Achieving growth rates of 5% and higher will depend on donor aid, as well as on the revival of the private sector through concrete steps by Israel to remove movement and access restrictions.

### III.B PRDP Progress and Prospects: PA Reforms

25. ***Even at the time of the Paris Donor Conference, the PA had advanced several reform commitments under the PRDP.*** These include early steps by the PA in mid-2007 to reverse the legacy of its past spending practices, including rehabilitating parts of the Public Financial Management System, and reconsolidating the Central Treasury Account (CTA), among others.
26. ***In administering its PRDP-linked Budget Support Trust Fund, and as part of the agreed mechanisms for PRDP monitoring, the World Bank in collaboration with the IMF has been in detailed discussions with the PA to assess progress to date with these reforms.*** In an effort to achieve fiscal sustainability, the PA has taken steps to control the public sector wage bill, including reducing public sector employment from 170,000 to less than 150,000 (a reduction by some 12%) and maintain its public sector hiring and wage bill cap. In addition, wage levels have remained the same throughout 2008. Moving forward, the PA commits to not exceed the agreed addition of 3,000 personnel per annum, mainly to the health and education sectors. Completing this issue will be a revisit of the pension system, to ensure that such a recruitment cap is in fact fiscally sound, based on reasonable public sector pensions.
27. ***Efforts to reduce net lending- the second largest expenditure, are critical.*** In early 2008, the PA directed municipalities to require "certificates of payment" of utility bills before providing certain services to the public, and has also continued expansion of the use of pre-paid meters in the West Bank. To date, over 4,000 meters have been installed. Efforts are also underway to remove local government control from the electricity distribution business by establishing autonomous distribution companies that operate on a commercial basis, including the recent establishment of the Northern Electric Distribution Company.<sup>23</sup> It is expected that this transfer of responsibility will be completed by the end of 2008. This is complemented by the adoption by the 132 municipalities of a new Unified Chart of Accounts, in an effort to increase transparency in municipal accounts. In addition to this, a Manual for Fixed Assets Registration has been prepared and is being used by municipalities in the West Bank. The benefits of these reforms will be greatest if matched by Israel's discontinuation of 'off-the-top' deductions of electricity bills owed to the Israeli Electricity Corporation (IEC) from the transfer of clearance revenues to the PA, as well as the adoption by the PA of an intergovernmental transfer system to mitigate the impacts on municipalities.

21 According to the Prime Minister's Office, 98 of these projects, with an average value of \$132,000, have been completed.

22 The economic results are based on joint analytical work using a model developed by Dr. Yousef Daoud of Birzeit University. The results also show that with a full amount of aid but no changes in movement and access restrictions, total real growth will be negative, averaging around -2% in 2008-2012. Also, if despite reforms, aid levels fail to meet the targets set out in the PRDP, growth will continue on its negative path and poverty levels will increase dramatically. Thus, Palestinian reforms taken alone will not reverse the economy's decline.

23 The IMF's March report notes that, as a result of these reforms, net lending is projected to be lower than estimated in the PRDP due to higher collection rates.

28. *These reforms should be complemented by a safety net mechanism that can properly target vulnerable persons and deliver assistance in a predictable way, and that can mitigate the impacts of the reforms above.* The Ministry of Social Affairs has begun a beneficiary verification program, as part of an overall targeting reform program. To date, 4,500 families have been verified, and 2,100 households regularly paid, under the World Bank-administered Social Safety Net Reform Program (SSNRP). It is expected that this verification program will continue to encompass 5,000 per quarter by end-2008, and increase bi-monthly cash assistance to 5,000 households by the end of the year, reaching an eventual target of 50,000.
29. *A primary component of the PRDP's pursuit of fiscal reform is the need to increase Government transparency and accountability through improved Public Financial Management.* In this regard, the 2008 budget was approved by the Cabinet on March 31<sup>st</sup>. The PA has also passed amendments to the Basic Finance Law establishing the Office of the General Accountant at the Ministry of Finance (MOF). The MOF has also launched a computerized accounting system, and has begun publishing monthly revenue and expenditure statements. Moving forward, it is critical for the MOF to establish and clarify procedures for its new accounting system, and to explore which regulations require changing to provide regulatory backing for this system. Full functioning of the office of the General Accountant would also enhance the reforms considerably.<sup>24</sup> Other steps may include the development of combined recurrent and development expenditures for each line ministry in time for the 2009 budget submission; strengthening the Central Treasury Account by closing non-zero balance accounts for recurrent expenditures; strengthening budget execution by preparing annual cash plans; and developing an internal audit plan.
30. *Furthermore, after a hiatus of over two years, efforts are underway to present a draft Procurement Law<sup>25</sup> and its accompanying regulations for approval by Presidential Decree in May 2008.* A draft law and set of regulations, reflecting substantial dialogue with a PA taskforce and civil society, was completed in 2006. Moving forward, the PA may find benefit in availing itself of international expertise in the preparation of national standard bidding documents, a manual of procedures, and the establishment of a Public Procurement Authority.
31. *Actions taken by the PA to date have added credibility to its policy agenda, but at the expense of additional strain on the economy, particularly in the face of lack of significant progress on the movement and access agenda.* As is the case elsewhere, the adoption of profound reforms is likely to incur costs for the population, particularly in the case of WB&G where parallel steps to trigger a private sector revival have not been taken. Thus, the absence of an enhanced security and trade environment will hamper the efforts by the PA to move away from its traditional role as income provider or to tackle key reforms to human resources, intergovernmental fiscal relations, and the current unaffordable pension system. For example, the recent PA policy of requiring proof of utility payments before extending certain municipal services has led to strikes by the Union of Public Employees and others on the basis that most are not able to pay under the current condition of the economy<sup>26</sup>. Nevertheless, reforms such as these are essential to the sustainability of Palestinian institutions. The credibility of the reform program itself will also benefit from adherence to agreed and announced steps, including the repayment of arrears in a way that does not deplete all the PA's resources and endanger its ability to service current expenditures. Finally, the delay of difficult but essential reforms to the unsustainable pension system will simply amplify the liabilities facing the PA in the future. Such reforms, if accompanied by a properly-structured safety net system, are achievable.

24 In this regard, the PA may wish to consider international assistance in capacity building and institutional strengthening, in order to benefit from international experience in this and other PFM reforms.

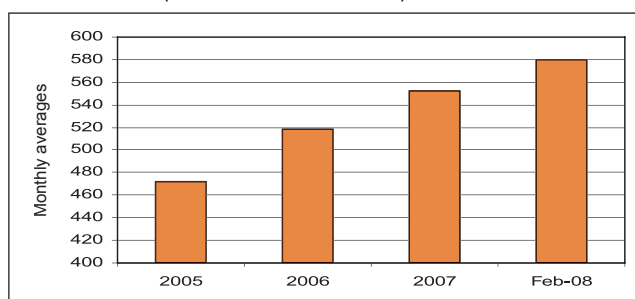
25 It must be noted that the current passing of laws through Presidential Decrees is due to the inability of the Palestinian Legislative Council to achieve quorum. However, once the PLC reconvenes, all laws mentioned will require the Council's approval to remain in effect.

26 At the time of this report, a High Court decision stopped implementation of the PA policy of requiring quit-claim certificates pending judicial review. However, the PA has noted that it has already collected a substantial amount of utility arrears, and continuing exploring acceptable policies to ensure continued payment of utility bills moving forward.

### III.C Progress and Prospects: Israeli Actions on Movement and Access

32. *With due regard to Israel's legitimate security concerns, it remains that the restrictions on movement of people and goods, and on access to natural and financial resources, continue to constrain economic activity in the WB&G.* World Bank analysis has shown that shrinking market access and hindered movement are the main constraints for Palestinian enterprises, as uncertainties in the delivery of inputs and products hike up costs.<sup>27</sup> The latest count of the number of obstacles before the movement of people and goods in the West Bank comes to 580, compared to a monthly average of 472 in 2005 (see Figure 4).<sup>28</sup> This is in addition to the continued construction of the Separation Barrier which isolates communities in 11.9% of the West Bank in enclosed enclaves, or between the barrier and the 1949 armistice line, and disrupts access between communities, markets, and services in nearby Palestinian communities.<sup>29</sup>

Figure 4: Obstacles in the West Bank  
(manned and unmanned)



Source: OCHA Humanitarian Situation Update, March 2008

33. *Since Annapolis, settlement activity has continued largely unabated, and in the case of the Jerusalem area has even been accelerated. Of the 885 settlement housing units tendered*

*in 2007, 747 were issued in the five weeks after Annapolis.*<sup>30</sup> Analysis of movement and access restrictions suggests that they primarily serve to expand and protect settlement activity and the movement of settlers and other Israelis in and out of the West Bank.<sup>31, 32</sup> Some 38% of the West Bank has been confiscated for current or future settlements and outposts and their growth as well as closed military areas, which has particularly constrained the economic space and resources available to Palestinians in Area C.<sup>33</sup> Palestinian use of public infrastructure, such as roads - of which 1,661 km is reserved for Israelis and settlers<sup>34</sup> - and telecommunications, to which Palestinians have yet to gain the use of frequencies allocated to for a second mobile operator, remain restricted. It is worth noting that the release of frequencies to the second mobile operator would result in an immediate injection of \$100-\$150 million in license fees to the PA, which would significantly reduce its current financial burdens over a one to two-month period.

34. *Obtaining permits for projects in Area C, whether for private, humanitarian or developmental purposes, is time consuming if not unattainable.*<sup>35</sup> Most NGOs report not having received construction permits since 2005. Particularly in the Jordan Valley, the lack of construction permits prevents several communities from developing or upgrading utilities (electricity, water) and social infrastructure (schools, clinics).<sup>36</sup> According to the Oslo Agreements, solid infrastructure requires approval by the Israeli authorities,

27 West Bank and Gaza Investment Climate Assessment, World Bank, March 2007.

28 Humanitarian Situation Update, OCHA, March 2008.

29 UN OCHA, "Preliminary Analysis of the Humanitarian Implications of the April 2006 Barrier Projections".

30 Compiled figures from Israel Lands Administration (ILA) and Ministry of Construction and Housing websites.

31 There are currently 149 settlements in the West Bank, including East Jerusalem, and roughly 110 outposts. The approximately 450,000 settlers living there are 63% more than at the time of the Oslo Accord in 1993. COGAT disputes these figures. They assert that there are 120 settlements in the Judea & Samaria region, accounting for 275,248 inhabitants. However, these figures do not include parts of municipal Jerusalem, which is the basis for OCHA's calculation.

32 COGAT asserts that these restrictions are also based on security considerations, and 'not necessarily' the growth of settlements in the West Bank, adding that many of the restrictions would be removed once the security environment improved.

33 OCHA, "Preliminary Analysis of the Humanitarian Implications of the Barrier Projections", April 2006.

34 COGAT notes that the Israeli authorities have invested NIS 1 billion in 'fabric of life' roads intended to provide adequate and effective solutions for Palestinians impacted by the current closures.

35 The Israeli Civil Administration requires an Israeli Masterplan to grant a permit for any construction or development project, but has not completed Masterplans for the vast majority of villages in Area C.

36 The Israeli authorities note some progress in kick-starting agribusiness initiatives in and around Jericho, including the proposed Japan-funded Agribusiness Park, where the Israeli authorities have approved capacity building initiatives for farmers in the area.



but humanitarian programs and temporary structures do not. Yet, several agencies have reported being forced to remove infrastructure for basic services (electricity, water, schools clinics), including temporary structures.

35. *Access to markets also continues to be completely severed in the Gaza Strip, and constrained through commercial crossings between the West Bank and Israel.* West Bank trade with and through Israel is administered by five commercial crossings.<sup>37</sup> Once the Barrier is complete, all trade with and through Israel will have to pass through them. The crossing points use a system of back-to-back cargo transfer similar to, but less cumbersome than, the system for crossing into Gaza. While it is still difficult to assess, initial reports from traders using the commercial crossing suggest that once all traffic is forced through these crossings, they may be unable to accommodate the current volume of traffic between Israel and the West Bank<sup>38</sup>. Palestinian businesses have already begun expressing serious concerns regarding the impact of the delays and additional costs entailed in using these terminals on their continued ability to compete. If the past experience at the similarly conceived Karni/ Al-Montar crossing between the Gaza Strip and Israel is any indication, these crossings could become the bottlenecks which constrain the economic development of the West Bank, much as the Karni crossing did to Gaza. An efficient and reliable crossing to and through Jordan, namely at Allenby Bridge, is seen by traders as necessary for direct market access from the West Bank. The recent Israeli decision

to extend the hours of operation in Allenby for the processing of people is a welcome step. However, Israel's removal of access restrictions on Palestinians into the Jordan Valley is a necessary precondition to develop an efficient and effective Jordan trade corridor.

36. *Israel's review of the current network of restrictions is essential, including restrictions on the use of natural resources and infrastructure.* It is recognized that Israeli has valid and undeniable security concerns. However, a balance must be struck between short-term security concerns and the potential to achieve long-term security and prosperity for both Israelis and Palestinians. This must be matched with PA policies that recognize the devastating impacts of short-term breaches in security. Recent announcements by the Israeli Government in April on the provision of 5,000 new permits for Palestinian construction workers to enter Israel; the reopening of several police stations; the issuance of 500 Businessmen Movement Cards; and the removal of 61 obstacles in the West Bank are welcome. Moving forward, it is imperative that these commitments are met in full. As UN OCHA has noted, only 44 of the 61 obstacles have been identified as removed, and of those, 5 are regarded as leading to tangible improvements in access for the Palestinian population.<sup>39</sup> Moreover, the facilitated entry and movement of regional participants in the upcoming Palestinian Investment Conference in Bethlehem in May will be an important milestone.

37 The main commercial crossings are Jalameh (north of Jenin), Bisan/Bardala (northern Jordan Valley), Irtah/"Sha'ar Efrayim" (south of Tulkarem; referred to as Taybeh), Beitunya (southwest of Ramallah), and Tarqumia (northwestern Hebron district).

38 In discussions with the PA, officials noted Israeli plans to channel all trade between Bethlehem and Jerusalem through the Tarqumia crossing, which will pose a significant bottleneck, with increased transportation and transactions costs.

39 UN OCHA presentation to donors, April 8th, 2008. According to OCHA, of the 61 checkpoints referenced, 6 were not removed and 11 were not recognized as having been in existence. Of the remaining 44, 17 were regarded as being insignificant (already removed, closed military zones, middle of a field, near a settlement), 9 were regarded as being of minimal significance (path to olive grove, unpopulated area, another obstacle nearby), and 13 were regarded as being very recently put in place by the IDF.

### III.D Progress and Prospects: The Donor Response and Strategies

37. *While the \$7.7 billion in aid pledged at the Paris Conference is significantly above the PRDP's requirements for 2008-10, its composition (in particular between support for the recurrent budget, public investment, and humanitarian assistance) is yet to be ascertained.* The 2008 budget approved on March 31<sup>st</sup> puts the required external budgetary support at \$1.634 billion and the development investment support at \$492 million.<sup>40</sup> However, only \$1.1 billion in recurrent budget support for 2008 was pledged in Paris, \$972 million in investment support, and \$651 million in humanitarian assistance. Thus, while the amounts pledged to development investments significantly exceed the PRDP budgeted needs, the amounts pledged to budgetary support in 2008 fall short.
38. *Donors have by and large followed through on their Paris pledges to recurrent expenditures, with nearly all donors who had pledged budgetary support having come through with all or some portion of their commitments.* Indeed, by April, about one-half of Paris pledges to recurrent expenditures had been disbursed.<sup>41</sup> The international community has also been responsive to PA needs by providing flexible mechanisms for support to recurrent expenditures. The EC took an important step in moving from the TIM mechanism to PEGASE, which provides channels for direct support to the CTA in addition to the types of channels used for TIM. The World Bank also launched a PRDP trust fund which would provide un-earmarked, untied support in the context of the PRDP's policy agenda. Furthermore, other donors availed themselves of direct disbursement to the PA's Central Treasury Account.
39. *Moving forward, remaining donor pledges will need to be transferred expediently to allow the PA a predictable flow of funds. Moreover, there remains a recurrent expenditure gap in 2008 that requires donors to convert their over-commitments to the development budget towards recurrent budgetary support.* Paris pledges towards recurrent spending are now about \$550 million less than the needs in 2008. At the same time, pledges towards development projects are about \$500 million in excess of the needs expressed in the PRDP. While the support of donors has allowed the PA to finance its deficits since December, it has only been able to do so in an ad hoc way, and at times having to rely on borrowings from the domestic banking sector.
40. *At the same time, the lack of predictable aid flows requires the PA to retain excess donor aid in any particular month, and smooth its spending patterns further in order to meet current spending needs over time.* During the fiscal crisis of 2006-07, the PA accumulated significant arrears in terms of public sector salaries, as well as private sector goods and services. In the PRDP, the PA committed to repayment of \$200 million in arrears in 2008. However, analysis suggests that the PA has in fact repaid larger amounts of arrears than it had committed to, which is likely to come at the expense of other current spending categories.
41. *On the development investment agenda, efforts are underway by donors and the PA to link the pledges to concrete project priorities identified in the PRDP.* Donor pledges at the Paris conference for development investments in 2008 totaled \$972.5 million, more than double the PRDP budgeted amount.<sup>42</sup> The Ministry of

40 These numbers are higher than the 2008 needs presented by the PA in Paris, due to changes in currency exchange rates (the 2008 budget was reframed at the exchange rate of 1 USD – 3.60 NIS) and other factors that have caused these external support figures to increase from \$ 1.361 billion and \$ 427 million for recurrent expenditure and development investment, respectively.

41 The EC, USA, Saudi Arabia, UAE, UK, Spain, Norway, France and the Netherlands have led donors in support to recurrent expenditures.

42 The PA had communicated that it does not intend to substantially expand the development agenda on the basis of this additional funding due to the absorptive capacity of its institutions, however preliminary lists of PRDP projects for 2008 reflect a total of \$696 million. While the PRDP allocations reflected expected disbursements in 2008, the PRDP project totals may in some cases reflect commitments rather than disbursements; this will require further clarification from the PA.

Planning is leading the effort to turn pledges into concrete projects, in collaboration with the line ministries that have prepared proposals under each of the 29 PRDP programs. The initial long-list of projects was presented in April, but will need to be rationalized, prioritized and reduced in order to meet the parameters of the 2008 budget and the three-year PRDP framework. Donors are currently in discussions with PA counterparts on this issue, and on specific projects. Due to the high level of pledges to development programs at Paris, funding is not likely to be a constraint. Rather, the challenge is related to technical issues and the ability to implement projects in Gaza. In addition, the level of disbursement in 2008 may be lower than planned due to the fact that the first quarter of the year has passed before commitments could be linked to the development agenda, which is still under development and discussion.<sup>43</sup> Moving forward, continued coordination between the PA and all donors through the unified channels of the local donor coordination mechanisms will be essential.

<sup>43</sup> *Donor commitments to the Governance agenda are limited to date.* Some support to the judiciary and the Office of the President has moved forward in 2008. The security sector has received special attention from donors interested in formulating the security program, but has yet to receive significant commitments. A conference has been organized in Berlin in April for consultations on the security program. Local government continues to be supported by the MDLF. *Donor commitments toward Economic Development have shown some progress in certain areas, most notably housing finance, trade facilitation, and SME development.* PIE, OPIC, IFC, Bank of Palestine, and DFID have committed \$500 million for AMAL, a new mortgage facility. USAID has indicated intentions to provide \$14 million towards commercial crossings with Israel. Donor programs will support SME development in 2008, including the new DFID/World Bank Enterprise Learning fund, the German PSD program, and a new USAID enterprise development fund. Still, the majority of proposed economic programs remain uncommitted. *Commitments to infrastructure projects are evident in water, sanitation, and electricity.* A number of wastewater treatment plants are under construction or have been committed. The electricity sector is a priority due to its relationship to net lending and is expected to receive significant support in 2008. Water is also a priority, although several projects that were committed earlier have yet to materialize due to movement and access restrictions. *The Social Development program has received significant support for social safety nets, but faces challenges in education and health.* Social protection is supported through PEGASE and the World Bank SSNRP, which cover payments to beneficiaries (nearly \$50 million, about half of the total beneficiary payments) as well as improvements in targeting. Efforts are underway to establish a sector-wide approach in education, which currently has over 20 active donors and nearly \$90 million in undisbursed commitments, with new commitments in 2008 still undetermined. Health is equally fragmented, and is in need of rationalization.

## IV. Conclusion

42. *As a tripartite action plan, the implementation of the PRDP has begun in earnest, but only partially.* The PA's three-year macroeconomic and fiscal framework assumes: (a) the successful advancement of fiscal and other reforms, including law and order; (b) sufficient and predictable donor funding to maintain operations and finance development programs; and (c) a gradual easing of movement and access restrictions by Israel. To date, the PA has engaged in fiscal reforms, which have been underwritten by donors in a substantial, albeit ad hoc, manner. However, the private sector revival required to trigger a virtuous cycle of growth has not been realized due primarily to continued restrictions on movement and access<sup>44</sup>.
43. *As a result, the economic scenarios presented at the Paris Conference, proposing that the implementation of Palestinian commitments alone is a necessary but insufficient condition for economic growth, have been confirmed by the zero GDP growth in the WB&G in 2007.* As for 2008, the IMF analysis notes a projected GDP growth of 3.0%. Taking into account population growth, it can be concluded that under the current movement and access restrictions, per capita incomes will drop or remain the same.
44. *Regardless of the scenario, PA reforms and sufficient donor support to both recurrent and development spending remain preconditions for Palestinian economic recovery.* The World Bank's previous analysis showed that a scenario where PRDP reforms continue, where they are fully funded by donors, and where private sector growth and trade is revived, will accelerate growth rates to double digit levels. Embedded in this scenario is a recovery in Gaza driven by the resolution of the current stalemate, and its immediate inclusion in the benefits of reforms, donor aid, and the lifting of movement restrictions. The analysis also shown that, even under the most optimistic scenarios, significant aid will continue to be needed. However, the ability of the private sector to resume its place as a driver for growth will have a major bearing on future aid requirements, which will therefore be even larger in the absence of improvements in movements and access restrictions.

<sup>44</sup> The Israeli authorities assert that, while an important factor, movement and access restrictions are not the only impediments. The enhancement of internal PA coordination is also a determinant.

# ANNEX 1:

## PA Policy Matrix for the World Bank-Administered PRDP-Linked Multi-Donor Trust Fund

Objectives	Prior Actions By May 2008	Indicators of Progress Next 12 Months (2008-2009)	Monitoring and Evaluation	Indicators of Progress 2009-11	Medium Term Objectives (PRDP Goals)
<b>I. Move toward Fiscal Sustainability</b>					
<b>I.1 Control Public Sector Wage Bill</b>	<ul style="list-style-type: none"> <li>Reduced budget financed employment from 170,000 to less than 150,000 by end December 2007</li> <li>No general wage increase for PA employees in 2008</li> </ul>	<ul style="list-style-type: none"> <li>PA employment does not exceed 153,000 anytime in 2008. New recruitment goes mainly to the Health and Education sectors</li> <li>No general salary increases for PA employees</li> <li>Initiate institutional review of public pension system</li> </ul>	<ul style="list-style-type: none"> <li>Ministry of Finance will provide the IMF and World Bank monthly pay roll reports and manual adjustments to determine total employment, average wage rates and which ministries receive new hires</li> <li>TOR for pension study to be agreed with the WB.</li> </ul>	<ul style="list-style-type: none"> <li>Total public employment does not grow by more than 3000 per year</li> <li>Establish HR management procedures that emphasize merit and performance as the basis for hiring and promotion in the civil service</li> <li>Complete the institutional review of the pension system</li> </ul>	<ul style="list-style-type: none"> <li>The wage bill declines from over 27% of GDP to less than 23% of GDP</li> <li>The PA has a strategy to deal with the pension crisis</li> </ul>
<b>I.2 Reduce Net Lending</b>					
<b>I.2a Institute measures to increase collection of electricity bills from users</b>	<ul style="list-style-type: none"> <li>Initiated program to rapidly introduce pre-paid meters in West Bank.</li> <li>Installed around 4000 pre-paid meters by May 2008</li> <li>Instituted a requirement that citizens present "certificates of payment" confirming their payment of utility bills to receive key government services.</li> </ul>	<ul style="list-style-type: none"> <li>Continue to expand the distribution of prepaid meters throughout the West Bank.</li> <li>Re-establish a culture of payment by continuing to require "certificates of payment" before delivering key government services</li> <li>Continue to develop programs to encourage payment of utility bills</li> </ul>	<ul style="list-style-type: none"> <li>Palestinian Energy Authority will report to World Bank energy team on number of meters installed. 2008 target is about 40,000 new meters</li> <li>World Bank energy team will track collection rates of electrical distribution companies</li> </ul>	<ul style="list-style-type: none"> <li>Continue to distribute pre-paid meters and require certificates of payment for public services</li> </ul>	<ul style="list-style-type: none"> <li>Electricity collection rates rise to about 90% on average in West Bank</li> </ul>

## Implementing the Palestinian Reform and Development Agenda

Objectives	Prior Actions By May 2008	Indicators of Progress Next 12 Months (2008-2009)	Monitoring and Evaluation	Indicators of Progress 2009-11	Medium Term Objectives (PRDP Goals)
<b>I.2b</b> Remove municipal and local governments from the electricity distribution business by establishing distribution companies (DISCO) that operate on a commercial basis	<ul style="list-style-type: none"> <li>Established the Northern Electric Distribution Company</li> </ul>	<ul style="list-style-type: none"> <li>By end 2008 all Electric Utilities in West Bank have time bound action plans, that are endorsed by the PA, to transfer the electricity departments of local governments including those that will be connected to the new feeder system</li> </ul>	<ul style="list-style-type: none"> <li>Plans will be submitted through the Palestinian Energy Authority for review by the World Bank power team</li> <li>World Bank energy team will review annual audits provided by the electric utilities</li> </ul>	<ul style="list-style-type: none"> <li>Local governments have transferred their electricity distribution to the utilities in accordance with the action plans</li> <li>All utilities investing in planned loss (technical and non-technical) reduction programs</li> <li>All electric utilities issue bills only in their name</li> <li>Audits for all electric utilities confirm their independent status</li> <li>Audits confirm that the flow of funds from electric utilities to their municipal owners are in accordance with their chart of accounts, e.g. dividends can not be paid until bills are cleared</li> </ul>	<ul style="list-style-type: none"> <li>Total net lending declines from around \$530 million currently to about \$400 million</li> <li>Electricity distribution throughout the West Bank is run on a commercial basis where distributors pay for all electricity they distribute</li> <li>Municipalities are no longer accumulating arrears to PA for electricity</li> </ul>
<b>I.2c</b> Improve targeting of social safety net to increase efficiency and ensure the most vulnerable populations are protected	<ul style="list-style-type: none"> <li>Started implementation of a beneficiary verification program aimed at improving targeting and preventing misallocation of social security funds.</li> <li>Verified at least 4,500 households in the targeting database</li> <li>Ministry of Social Affairs initiated regular assistance payments to 2,100 households through the new social safety net pilot program</li> </ul>	<ul style="list-style-type: none"> <li>Increase home visits to verify targeting database to 5,000 per quarter by end 2008</li> <li>Increase regular bi-monthly cash assistance payments to 5,000 households by end of 2008</li> </ul>	<ul style="list-style-type: none"> <li>The Ministry of Social Affairs provides the Bank team with regular monthly reports on progress in building the verified database and providing payments to verified households</li> </ul>	<ul style="list-style-type: none"> <li>Begin a process of merging on-going cash assistance programs using targeting database to confirm eligibility</li> <li>Complete a Social Protection Strategy</li> </ul>	<ul style="list-style-type: none"> <li>A fully functioning targeting database with at least 50,000 verified households guides all assistance programs no matter what the source of funding</li> <li>The PA institutes a Social Protection Reform and Integration Program that coordinates all social protection initiatives and ensures uniform payment modalities and amounts</li> </ul>



Objectives	Prior Actions By May 2008	Indicators of Progress Next 12 Months (2008-2009)	Monitoring and Evaluation	Indicators of Progress 2009-11	Medium Term Objectives (PRDP Goals)
<b>I.2d</b> Increase financial accountability through improved and more transparent municipal accounts	<ul style="list-style-type: none"> <li>Established a Unified Chart of Accounts for municipalities and finalized a budget manual that is now being used by municipalities in the West Bank</li> <li>Finalized a fixed assets registration manual that is being used by municipalities in West Bank</li> </ul>	<ul style="list-style-type: none"> <li>Finalize pilot financial management information system for small, medium and large municipalities that will be tested and rolled out.</li> </ul>	<ul style="list-style-type: none"> <li>Bank team supporting the MDLF program will track implementation of municipal financial management information system</li> </ul>	<ul style="list-style-type: none"> <li>Rollout the municipal financial information management system across the West Bank</li> <li>Introduce a standard annual audit of municipal accounts based on international standards</li> <li>MDLF develops clear criteria for performance based transfers to municipalities</li> </ul>	<ul style="list-style-type: none"> <li>Palestinian local governments producing transparent accounts that are audited according to international standards</li> </ul>
<b>II Increase Government Transparency and Accountability Through Improved Public Financial Management</b>					
<b>II.1</b> Establish upgraded institutional and regulatory procedures to support PFM reforms	<ul style="list-style-type: none"> <li>Passed amendments to the Basic Finance Law establishing a Office of the General Accountant in the Ministry of Finance</li> <li>Launched a new computerized accounting system in the Ministry of Finance</li> </ul>	<ul style="list-style-type: none"> <li>Prepare and approve a design paper for the new computerized accounting system processes and procedures</li> <li>Amend financial regulations and related internal documents to provide the regulatory backing for the new computerized accounting system</li> <li>Operationalize the Office of General Accountant</li> </ul>	<ul style="list-style-type: none"> <li>The World Bank will recruit a governance advisor who is also a PFM expert to be resident in WBG. He will work closely with the IMF to monitor development of the new computerized system and provide advice on its implementation</li> </ul>	<ul style="list-style-type: none"> <li>Roll out computerized accounting system through out government, starting with the Ministry of Education and then extending to all line ministries</li> </ul>	<ul style="list-style-type: none"> <li>A fully computerized accounting system used through out the government, which will allow the PA to dramatically improve its accounting procedures and budget preparation process in line with acceptable international practice.</li> </ul>
<b>II.2</b> Improve efficiency and transparency of the budget preparation process	<ul style="list-style-type: none"> <li>2008 budget approved</li> <li>Ministry of Finance began publishing monthly expenditure and revenue statements</li> </ul>	<ul style="list-style-type: none"> <li>Develop a combined presentation of the recurrent and development budgets for each line ministry for the 2009 Annual Budget Law</li> </ul>	<ul style="list-style-type: none"> <li>Budget information is publicly available and will be tracked by Bank PFM expert</li> </ul>	<ul style="list-style-type: none"> <li>For pilot ministries, develop program budgets based on simple program structures</li> <li>Develop a plan for transfer of responsibility for development budgets to Ministry of Finance</li> </ul>	<ul style="list-style-type: none"> <li>Establish a government wide system that will allow annual budgets to be developed on time in a transparent manner</li> </ul>

## Implementing the Palestinian Reform and Development Agenda

Objectives	Prior Actions By May 2008	Indicators of Progress Next 12 Months (2008-2009)	Monitoring and Evaluation	Indicators of Progress 2009-11	Medium Term Objectives (PRDP Goals)
<b>II.3</b> Strengthen PFM infrastructure and improve auditing functions		<ul style="list-style-type: none"> <li>Strengthen Central Treasury Account by closing non-zero balance line ministry and agency bank accounts for recurrent expenditures</li> <li>Prepare annual cash plans for guiding budget execution</li> <li>Develop an internal audit plan/ produce selective audit reports</li> </ul>	<ul style="list-style-type: none"> <li>The Bank PFM specialist will work closely with his IMF counterparts to both assist the PA in carrying out these tasks and to monitor their progress. These tasks are centralized in the Ministry of Finance which will allow them to be tracked easily in the quarterly World Bank/IMF reviews of reform progress</li> </ul>	<ul style="list-style-type: none"> <li>Pilot commitment control procedures in the Ministry of Finance and Ministry of Education</li> <li>Extend the new commitment control procedures to other ministries in conjunction with the roll out of the new computerized accounting system</li> <li>Introduce monthly reporting of outstanding commitments</li> <li>Comply with the reporting requirement of the Financial Regulations starting with the production of audited consolidated financial statements for 2008 in 2009</li> <li>Develop a plan to adopt an economic classification to be consistent with the GFSM 2001 framework</li> <li>FACB applies best practice external audit methodology and responds to public complaints</li> </ul>	<ul style="list-style-type: none"> <li>A strong Central Single Treasury Account continues to operate</li> <li>Have a functioning cash planning and management system</li> <li>Have a fully developed budget classification system</li> <li>PA has a strong system of external audits</li> </ul>