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**Report on UNCTAD assistance to the Palestinian people**

## **Report on UNCTAD assistance to the Palestinian people: Developments in the economy of the Occupied Palestinian Territory**

**Note by the UNCTAD secretariat\*, \*\***

### *Summary*

In 2021, the gross domestic product (GDP) of the Occupied Palestinian Territory grew by 7.1 per cent, following a contraction by 11.3 per cent in 2020 due to the pandemic and continued restrictive measures under occupation. The growth reflected low base effects and failed to make up for income lost in 2020, as GDP in 2021 remained below the pre-pandemic level of 5.1 per cent in 2019. The rebound was restrained by a decline in foreign aid; the impact of the military operation in the Gaza Strip in May 2021; and a protracted fiscal crisis.

Occupation distorts the Palestinian economy and enforces de-agriculturalization and deindustrialization. Settlements continued to expand and the demolition of Palestinian assets in the West Bank was at a five-year high in 2021. Socioeconomic conditions worsened, food insecurity increased, unemployment remained high and over one third of households fell below the poverty line. Meanwhile, the costly economic, trade-related and labour market dependence on the economy of Israel deepened.

The deterioration in economic and political conditions fostered a deep fiscal crisis characterized by a steep decline in donor aid, a large financing gap and the build-up of potentially destabilizing domestic debt and arrears to the private sector and pension fund.

In May 2021, Gaza was subjected to a significant military operation that inflicted serious damage on an already shattered infrastructure. Over half of the workforce was unemployed in 2021, 83 per cent of workers received less than the minimum wage and 60 per cent of the population was classified as poor.

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\*\* This report should not be quoted by the press before 14 September, 5 p.m. GMT.



## I. Uneven recovery

1. Since 2020, the Occupied Palestinian Territory has witnessed several waves of the pandemic, to which the Palestinian government responded by introducing lockdown measures of varying severity and duration. A sharp decline in economic activity followed; the economy of the Occupied Palestinian Territory contracted by 11.3 per cent in 2020, the second largest contraction since the establishment of the Palestinian National Authority in 1994.
2. The socioeconomic impact of the pandemic in the Occupied Palestinian Territory has not been unique, but the systematic barriers imposed under occupation and the lack of fiscal and monetary policy space have deprived the Palestinian government of the policy tools available in other countries to mitigate the fallout and accelerate recovery. The impact of the pandemic has reached beyond the poor; 72 per cent of households in the West Bank reported income losses, compared with 57 per cent of households in Gaza. Meanwhile, food insecurity increased from 9 to 23 per cent in the West Bank and from 50 to 53 per cent in Gaza.<sup>1</sup>
3. Following vaccination campaigns and a decline in cases, restrictions were gradually eased and business activity edged towards normal. In 2021, GDP grew by 7.1 per cent, yet such growth was not sufficient to make up for the income lost in 2020. Real GDP in 2021 was below the level in 2016 and 5.1 per cent below the pre-pandemic level in 2019.
4. The scope of the rebound was limited by a decline in foreign aid, the military operation in Gaza in May 2021 and a protracted fiscal crisis. The partial recovery has been concentrated in the West Bank, with a growth rate of 7.8 per cent. Gaza lagged, at a rate of 3.4 per cent, and regional divergence widened. Except for in agriculture, performance in all sectors improved. Value added in the construction, industrial and services sectors grew by 8, 5.5 and 5 per cent, respectively. However, the agricultural sector contracted by 3 per cent, extending a long-term declining trend.<sup>2</sup>
5. As the low base effects that underpinned growth in 2021 fade, if the status quo persists, GDP growth is expected to be in the range of 3 per cent in the medium term, barely enough to keep up with a growing population and implying weak labour markets and per capita GDP stagnation.<sup>3</sup> However, the deterioration in global economic prospects in the first half of 2022 has put the prospects firmly on the downside.
6. Inflation in the Occupied Palestinian Territory has been below 2 per cent in recent years and, due to the pandemic, turned negative in 2020. However, with recovery under way, a modest price inflation returned, at 1.2 per cent in 2021. With the recent global rise in energy and food prices, there is a risk of greater inflationary pressures and food insecurity in 2022, particularly as most of the wheat consumed in the Occupied Palestinian Territory is imported from the Russian Federation and Ukraine, either directly or indirectly via Israel. The decline in the number of tourists from the Russian Federation, the third largest group of visitors to the West Bank, is another negative spillover of the war in Ukraine.

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<sup>1</sup> World Bank, 2022, Economic monitoring report to the Ad Hoc Liaison Committee, May.

<sup>2</sup> Palestinian Monetary Authority and Palestinian Central Bureau of Statistics (PCBS), 2021, The performance of the Palestinian economy during 2021, as well as the economic forecasts for the year 2022, available at <https://pcbs.gov.ps/site/512/default.aspx?lang=en&ItemID=4148>.

*Note:* All websites referred to in footnotes were accessed in July 2022.

<sup>3</sup> Ibid.

7. Rooted in occupation, the persistent economic crisis in the Occupied Palestinian Territory predates the pandemic. Average income has been on a declining trend since 2016. GDP per capita grew by 4.2 per cent in 2021, compared with in 2020 (see table), but this is a low base effect that followed a 13.5 per cent contraction in 2020. In 2021, GDP per capita remained at not only below the level in 2019, but also below that in 2011, reflecting a decade of worsening political horizons and lost development opportunities. Compared with regional peers, in 2021, Palestinian per capita GDP at purchasing power parity was \$5,394, equivalent to 47 per cent of per capita GDP in Egypt, 58 per cent in Lebanon, 57 per cent in Jordan and 14 per cent in Israel.<sup>4</sup>

### Economy of the Occupied Palestinian Territory: Key indicators

	1995	1999	2002	2006	2010	2014	2019	2020	2021*
<b>Macroeconomic performance<sup>a</sup></b>									
Real GDP growth (percentage)	7.1	8.3	-12.5	-1.0	5.8	-0.2	1.4	-11.3	7.1
GDP, nominal (millions of dollars)	3 283	4 271	3 556	5 348	9 682	13 990	17 059	15 532	18 037
Gross national income (millions of dollars)	3 723	5 025	3 775	5 771	10 281	15 472	19 717	18 107	21 435
Gross national disposable income (millions of dollars)	4 122	5 398	4 826	7 062	12 272	17 138	21 726	19 941	23 615
GDP per capita, nominal (dollars)	1 427	1 553	1 182	1 578	2 559	3 357	3 641	3 234	3 655
Gross national income per capita, nominal (dollars)	1 618	1 827	1 255	1 703	2 718	3 713	4 208	3 770	4 344
Real GDP per capita growth (percentage)	-0.2	4.8	-15.0	-4.0	3.1	-2.5	-1.2	-13.5	4.2
Real gross national income per capita growth (percentage)	0.7	4.6	-16.4	-2.7	0.6	-1.2	-0.9	-15.1	6.6
<b>Population and labour</b>									
Population (millions) <sup>b</sup>	2.34	2.96	3.23	3.61	4.05	4.55	4.98	5.10	5.41
Unemployment (percentage) <sup>c</sup>	18.2	12.0	31.2	23.7	23.7	26.9	33.0	36.0	26.0
Total employment (thousands)	417	588	452	636	743	913	1 010	956	1 034
In public sector	51	103	105	147	178	209	210	201	208
In Israel and settlements	68	135	42	55	78	107	133	125	145
<b>Fiscal balance (percentage of GDP)</b>									
Revenue net of arrears/clearance withheld	13.0	23.4	8.2	25.0	19.9	20.1	20.3	22.1	23.5
Current expenditure	15.0	22.1	28.0	42.6	31.8	29.6	25.6	30.8	29.1
Total expenditure	25.1	29.3	34.2	48.3	36.4	31.5	27.6	32.6	30.4
Overall balance (commitment basis)	-12.1	-5.9	-26.0	-23.3	-16.5	-11.4	-7.3	-10.5	-7.0
Public debt <sup>d</sup>	..	20.0	21.1	20.4	19.4	15.8	16.4	23.5	21.3
<b>External trade</b>									
Net current transfers (millions of dollars)	400	373	1 051	1 291	1 991	1 405	1 545	1 141	1 789
Exports of goods and services (millions of dollars)	562	752	478	1 046	1 639	2 320	2 631	2 336	2 775
Imports of goods and services (millions of dollars)	2 441	3 364	2 234	5 263	5 793	6 929	8 376	7 189	8 382
Trade balance (millions of dollars)	-1 879	-2 612	-1 756	-4 218	-4 154	-4 610	-5 746	-4 853	-5 607
Trade balance (percentage of GDP)	-57.2	-61.2	-49.4	-78.9	-42.9	-33.0	-36.3	-34.6	-37.3
Trade balance with Israel (millions of dollars)	-922	-1 598	-886	-1 887	-2 737	-2 869	-3 788	-3 373	-4 188
Trade balance with Israel (percentage of GDP)	-28.1	-37.4	-24.9	-35.3	-28.3	-20.5	-22.2	-21.7	-23.2
PNA trade with Israel/total PNA trade (percentage) <sup>e</sup>	83.5	67.5	56.9	46.3	59.9	63.0	63.9	66.8	71.2
PNA trade with Israel/total Israeli trade (percentage) <sup>e</sup>	4.2	3.8	1.9	2.3	2.7	3.1	3.4	3.2	3.2

Sources: Palestinian Ministry of Finance and Planning, Palestinian Monetary Authority and PCBS. The source of data on trade with Israel is the Central Bureau of Statistics of Israel.

Abbreviation: PNA, Palestinian National Authority.

\* Preliminary estimates.

<sup>a</sup> In 2019, PCBS revised national accounts data from 2004 onwards.

<sup>b</sup> Except for population figures, all data exclude East Jerusalem, due to the fact that PCBS has no access to the city.

<sup>c</sup> In 2019, PCBS began to apply the guidelines of the nineteenth International Conference of Labour Statisticians. The stability of the unemployment rate in the last few years reflects weak labour market participation.

<sup>d</sup> Includes domestic and external debt but not arrears or government debt to the pension fund.

<sup>e</sup> Israeli and Palestinian trade data refer to goods and non-factor and factor services.

<sup>4</sup> See <https://data.worldbank.org/indicator/NY.GDP.PCAP.PP.CD>.

## A. Enduring poverty and unemployment crises

8. Despite the economic rebound in 2021, unemployment in the Occupied Palestinian Territory remained high, at 26 per cent. In Gaza, over half the workforce remained unemployed, the average wage was 48 per cent of the counterpart in the West Bank and 83 per cent of workers received less than the monthly minimum wage (\$435). In the West Bank, unemployment reached 17 per cent, with 7 per cent of the workforce paid below the minimum wage, implying that 28 per cent of Palestinian workers receive less than the minimum wage.<sup>5</sup>

9. High unemployment levels and low wages translate into deeper and wider poverty. The latest Palestinian expenditure and consumption survey (2016/17) indicates that 29.3 per cent of the population live below the poverty line of \$5.5 per day. However, World Bank simulations suggest that recent economic deterioration and the pandemic have increased poverty to 35.6 per cent of the population.<sup>6</sup> In Gaza, 60 per cent of the population live below the poverty line. Palestinians in East Jerusalem are marginalized and experiencing high levels of poverty although they are fully under administration by Israel. In 2019, 72 per cent of Palestinians in East Jerusalem were classified as poor, compared with 26 per cent of Israelis.<sup>7</sup>

10. Dire socioeconomic conditions are summarized by the high unemployment level, even with a low level of labour force participation (44 per cent) and a large informal sector that accounts for 60 per cent of the workforce and in which most employees receive less than the minimum wage. The dominance of low-pay informal employment explains why many employed Palestinians are classified as poor.

11. In an environment of security crises and exposure to frequent external economic and political shocks, Palestinians are vulnerable to even small decreases in expenditure and income. A 5 per cent fall in expenditure in the West Bank could increase poverty by as much as 16 per cent and a 15 per cent fall could increase poverty by as much as 50 per cent.<sup>8</sup>

## B. Palestinian workforce dependency on precarious employment in Israel and settlements

12. The weak capacity of the Palestinian economy for job creation, under occupation, leaves no choice for a large share of workers but to seek employment in Israel and settlements. The long-standing tendency of the Occupied Palestinian Territory to serve as a reservoir of cheap labour for the economy of Israel has accelerated in recent years. Employment in Israel and settlements has more than doubled since the establishment of the Palestinian National Authority despite the exclusion of the workforce of Gaza from employment in the economy of Israel since 2007. The majority of Palestinians are employed as unskilled workers in construction, agriculture, fishing and forestry, mining, quarrying and low-technology manufacturing.

13. By early 2022, the number of Palestinians employed in Israel and settlements had reached 153,000, or one fifth of the employed labour force of the West Bank.<sup>9</sup> Employment in Israel and settlements generates significant income for workers from the West Bank, who earn close to \$3 billion per year, about one quarter of the West Bank GDP. Consequently, the economy of the West Bank is dependent on income earned in Israel and settlements to support aggregate demand in all sectors of the Palestinian economy.

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<sup>5</sup> Palestine Economic Policy Research Institute (MAS), 2021a, Economic Monitor 67, available at <https://mas.ps/en/publications/5958.html>.

<sup>6</sup> World Bank, 2022.

<sup>7</sup> MAS, 2021b, Prospects for development in Palestine, available at [https://mas.ps/development\\_reports/download/2022/04/22/development-report-eng-1650653647.pdf](https://mas.ps/development_reports/download/2022/04/22/development-report-eng-1650653647.pdf).

<sup>8</sup> A Atamanov and N Palaniswamy, 2018, West Bank and Gaza: Poverty and shared prosperity diagnostic 2011–2017, World Bank.

<sup>9</sup> Office of the Special Coordinator for the Middle East Peace Process, 2022, Report to the Ad Hoc Liaison Committee, May.

14. Palestinians employed in Israel and settlements are subject to decent work deficits, including long commutes, long waits at crossings, a lack of social protection and inadequate working conditions. Furthermore, a permit system has led to the exploitation of Palestinian workers by brokers and employers wielding undue power. The International Labour Organization estimates that brokers earn over \$119 million in annual profits through the permit system.<sup>10</sup>

15. Empirical research suggests that employment in Israel and settlements leads to a variety of negative impacts on Palestinian GDP growth.<sup>11</sup> Such employment undermines the competitiveness of the Palestinian economy by dampening incentives to invest in human capital, decreasing the supply of skills and increasing domestic wages without a corresponding growth in productivity. Furthermore, such employment is unpredictable, precarious and sensitive to political and security crises. It cannot be a substitute for rejuvenating the Palestinian labour market by lifting the blockade on Gaza and lifting all economic restrictions throughout the Occupied Palestinian Territory.

### C. Electricity and water: Dependence, shortage and high cost

16. In both the West Bank and Gaza, there are significant gaps in water supply, estimated at 33 and 102 million cubic metres per year, respectively.<sup>12</sup> Palestinians must therefore import water from Israel at a high cost, yet supply still falls short of demand in both the West Bank and Gaza. In the West Bank, water accounts for 8 per cent of the average income of Palestinian households, much higher than global norms. Meanwhile, poor households not connected to the water network pay up to 17 per cent of family income to purchase water.<sup>13</sup> On average, the daily consumption of water by Palestinians connected to a water network is below the minimum recommended by the World Health Organization and is about one third of the daily consumption rate of water in Israel.<sup>14</sup>

17. Water shortages not only constrain agricultural development, but also impact public health and limit growth opportunities in manufacturing and other sectors, directly or indirectly, by eliminating potentially important forward and backward linkages.

18. The Occupied Palestinian Territory produces just 3 per cent of the electricity consumed and imports 90 per cent from Israel. The cost of electricity therefore reflects the tariff of the Israel Electric Corporation, one of the highest in the region. The consequences are evident for Palestinian producers and households, who spend 9 per cent of expenditures on electricity, a rate twice that in Egypt and Lebanon and three times that in Jordan.<sup>15</sup>

19. West Bank electricity demand has exceeded 1,200 MW and is expected to increase by over 270 MW per year by 2030. In Gaza, the blockade, repeated destruction of infrastructure and shortage of fuel have resulted in a significant electricity shortage; average demand exceeds 400 MW and peak demand routinely reaches 550 MW, while supply is in the range of 190 MW, meeting 48 and 35 per cent of average and peak demand, respectively. About 63 per cent of the electricity supply in Gaza is imported from Israel; the power plant in Gaza supplies the rest.<sup>16</sup>

<sup>10</sup> International Labour Organization, 2020, The situation of workers of the occupied Arab territories, available at [https://www.ilo.org/wcmsp5/groups/public/---ed\\_norm/---relconf/documents/meetingdocument/wcms\\_745966.pdf](https://www.ilo.org/wcmsp5/groups/public/---ed_norm/---relconf/documents/meetingdocument/wcms_745966.pdf).

<sup>11</sup> J Agbahey, K Siddig and H Grethe, 2016, Access to Israeli labour markets: Effects on the West Bank economy, available at <https://econpapers.repec.org/paper/agsiamf16/243992.htm>.

<sup>12</sup> Office of the Quartet, 2022, Report to the Ad Hoc Liaison Committee, May.

<sup>13</sup> MAS, 2021a.

<sup>14</sup> See <https://switchmed.eu/wp-content/uploads/2020/12/2020.11.30-Country-Profile-Palestine.pdf>.

<sup>15</sup> Ibid.

<sup>16</sup> Office of the Quartet, 2022.

20. The electricity shortage in Gaza restricts availability to half the day and undermines the delivery of essential public services, including water, health and sanitation. Hospitals must operate at well below capacity in a context of growing demand for services due to the pandemic and restrictions on travel to seek medical care outside Gaza, as well as due to military operations. The shortage has also led to the dumping of untreated wastewater into the sea, with negative consequences for public health, fishing yields and entertainment possibilities.

#### **D. Impaired competitiveness, de-agriculturization, deindustrialization and de-development**

21. Gaza has remained under blockade since 2007 and in the West Bank, the occupying Power maintains a stringent system of administrative and physical restrictions on the movement of Palestinian people and goods, including a permit regime, hundreds of permanent and flying checkpoints, gates, earth mounds, roadblocks and trenches.

22. Occupation deprives Palestinian producers of unhindered access to regional and global markets, which is essential for a small economy, consisting of just over 5 million people, with weak purchasing power. Furthermore, occupation fragments the Palestinian economy into three separate zones in the Gaza Strip and the West Bank, including East Jerusalem, with further fragmentation within the West Bank. The result is an archipelago economy, some areas of which approach autarky, with individual areas reduced to small-size inefficiency and unable to benefit from economies of scale.

23. In accessing internal and external markets, Palestinians face additional costs arising from longer, more expensive transportation routes, security inspections, delays and storage fees. The additional costs impair the competitiveness of producers and pre-empt the realization of benefits from international trade and integration into regional and global value chains.

24. Adaptation to restrictions under occupation entrenches import and aid dependence and fosters a weak export sector characterized by a high degree of concentration and low technology content, with 10 labour-intensive products accounting for two thirds of total exports. The resulting distorted, inward-oriented productive structure features an enlarged share of the non-tradable goods (services) sector and a smaller share of the tradable goods (agricultural and industrial) sector. Meanwhile, the bulk of employment generation has been taking place in activities with low labour productivity, sometimes as low as one fifth of the productivity of better performing sectors.<sup>17</sup>

25. The growing share of the services sector diverges from that of regional comparators and is not compatible with the Palestinian level of development. This structural distortion reflects a process of path-dependent adaptation to restrictions imposed under occupation, which disproportionately impact the tradable goods sector. Such adaptation limits growth prospects because the limited tradable goods sector typically has higher productivity growth and a greater capacity for innovation and the generation of more decent, better paying jobs.

26. Palestinian competitiveness is further weakened by the lack of a national currency and use of the new shekel, the exchange rate of which reflects the needs and level of development of the more advanced economy of Israel. Furthermore, the employment of Palestinian workers in Israel and settlements exerts upward pressure on domestic wages without corresponding productivity gains. The fact that two of the most important prices in any economy are either fully (exchange rate) or largely (wages) determined in Israel further constrains the competitiveness of Palestinian producers in the domestic and export markets.

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<sup>17</sup> MAS, 2021b.

27. The West Bank accounts for nearly all Palestinian exports. Exports from Gaza have been virtually reduced to zero under the blockade. Meanwhile, imports remain high (47 per cent of GDP in 2021) and most are financed by remittances, aid and income from employment in Israel and settlements. Exports covered just one third of the import bill, leading to a significant trade deficit in 2021 (37 per cent of GDP), among the highest in the world. The stifled competitiveness of Palestinian producers explains both sides of the trade deficit, namely, low levels of exports and a large import bill.

28. By limiting Palestinian access to global markets, occupation ensures a deep trade dependence on Israel that precludes potentially substantial advantages from diversifying trade partners. Efforts by the Palestinian government to diversify trade partners have not been successful despite agreements giving Palestinians privileged access to the large markets of the United States of America, the European Union and the Southern Common Market (Mercosur), as well as among members of the Greater Arab Free Trade Area. In 2021, Israel accounted for 72 per cent of Palestinian trade, while the share of the Palestinian market in total Israeli trade was just 3 per cent.

29. Furthermore, the additional costs imposed under occupation place Palestinian producers at a stark disadvantage compared with competitors in Israel with free access to Palestinian markets in accordance with the stipulations of the Paris Protocol,<sup>18</sup> who thereby successfully capture much of the Palestinian market. In 2021, the bilateral Palestinian trade deficit with Israel exceeded 23 per cent of GDP. However, porous borders and smuggling activities suggest that this deficit could be much greater.

30. Restrictions on movement obstruct the delivery of essential social services and humanitarian relief and impinge on the right of Palestinian people to health, work, education and decent living, among other human rights. Women are disproportionately affected by such restrictions, which undermine their right to equal labour market participation and hinder their access to health and education services. Women also face additional safety concerns during commutes and at checkpoints, which lead many to work from home or near home or to remain unemployed.

31. Although Palestinian women have better education rates and more years of schooling compared with men, in 2021, 54 per cent of women were unemployed compared with 30 per cent of men and 35 per cent of youth (aged 15–29). Meanwhile, on average, women earned 20 cents of gross national income for every dollar earned by men. A significant part of the gender-related employment and income gap is directly due to occupation.<sup>19</sup>

32. The Palestinian economy has undergone a deep structural distortion, through long-term de-agriculturalization, deindustrialization and de-development. In 1994–2021, in the Occupied Palestinian Territory as a whole, the share of agriculture in GDP declined from 12.1 to 6.5 per cent, the share of industries declined from 22 to 12 per cent and the share of services grew from 60 to 77 per cent. In Gaza, the share of agriculture stagnated, the share of industries declined from 22 to 7 per cent and the share of services rose from 61 to 78 per cent. In the West Bank, the share of agriculture declined from 13.6 to 5.8 per cent, the share of industries declined from 22 to 13 per cent and the share of services rose from 59 to 76 per cent.

33. Obstacles to agricultural development include the expropriation of land and water; restrictions on the importation of inputs and fertilizers; and the destruction of agricultural facilities and crops. Area C, which accounts for over 60 per cent of West Bank area and contains the richest land and natural resources, remains under occupation and settlements control 85 per cent of the water resources. Meanwhile, the Separation Barrier traps 10 per cent of the agricultural land of the West Bank in the area between the barrier and the Green Line (corresponding to the June 1967 border), or seam zone.

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<sup>18</sup> A/49/180, Annex IV, Protocol on economic relations between the Government of the State of Israel and the Palestine Liberation Organization, representing the Palestinian people.

<sup>19</sup> MAS, 2021b; World Bank, 2022.

34. The barrier and associated control system limit access by Palestinian farmers to the land inside the zone and foster significant productivity and output losses. For example, the barrier serves to make olive trees in the seam zone half as productive as trees on the other side.<sup>20</sup> Not only has the agricultural sector underperformed at an aggregate level, but productivity has also lagged significantly behind that of regional comparator and is a small fraction of that of Israel despite nearly identical climatic and soil conditions. For example, yields per area in the Occupied Palestinian Territory are about 43 per cent of those in Israel and half those in Jordan.<sup>21</sup>

35. In Gaza, the occupying Power has established a “buffer zone” extending 300–1,500 metres from the fence separating Gaza from Israel, covering roughly 17 per cent of the total area of Gaza and rendering over 35 per cent of agricultural land inaccessible to Palestinian producers.<sup>22</sup>

36. The military operation that took place in Gaza in May 2021 devastated agricultural land, crops, orchards, livestock sheds, greenhouses, fruit trees, storage facilities, boats, fishing equipment, agribusinesses, irrigation canals and water pumping systems. Greenhouses sustained the greatest damage, which will have significant implications due to their higher crop yields in a context of limited access to land and water.<sup>23</sup> The recovery of agriculture in Gaza will be prolonged if the restrictions imposed under occupation on the importation of equipment and essential materials persist.

## **E. Settlements expanding and demolition of Palestinian assets peaking**

37. Settlements continued to expand in 2021. However, the United Nations, in several resolutions, including the Security Council in its resolution 2334 (2016), has reaffirmed that the establishment of settlements constitutes a flagrant violation under international law. By November 2021, there were more than 138 settlements recognized by the Government of Israel and 150 unrecognized “outposts”. Although outposts are nominally illegal under Israeli law, they are, for all intents and purposes, settlements, as they are permitted to exist although more than one third have been fully or partially built on land acknowledged by the Government of Israel as privately owned by Palestinians. Outposts are given security, as well as sophisticated infrastructure provided by the Government, and some are later regularized as part of official settlements.<sup>24</sup>

38. Palestinians in Area C are subjected to settler violence, including the destruction of residential and humanitarian structures, physical assault, intimidation, the use of live ammunition, the uprooting and destruction of trees and crops and the vandalization of farming equipment and private property. In some instances, settlements discharge sewage water onto Palestinian land, causing pollution and damage to water and productive trees. In 2021, the Office for the Coordination of Humanitarian Affairs documented the highest level of settler violence since 2005, which undermined the ability of Palestinians to carry out essential agricultural work and other economic activities. About 500 attacks by settlers resulted in death, injuries and extensive property damage.

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<sup>20</sup> TD/B/67/5.

<sup>21</sup> UNCTAD, 2015, *The Besieged Palestinian Agricultural Sector* (United Nations publication, New York and Geneva).

<sup>22</sup> See <https://www.amnesty.org/en/latest/news/2022/02/israels-apartheid-against-palestinians-a-cruel-system-of-domination-and-a-crime-against-humanity/>.

<sup>23</sup> Food and Agriculture Organization of the United Nations, 2021, *Impact of the May Conflict Escalation on the Agricultural Area in the Gaza Strip*, Rome.

<sup>24</sup> B’Tselem, 2021, *State Business: Israel’s Misappropriation of Land in the West Bank Through Settler Violence*, Jerusalem.

39. The occupying Power fully controls Area C, which represents over 60 per cent of West Bank area. It is extremely difficult for Palestinians to obtain permits to build structures for residences, economic activities or infrastructure such as roads and water and power networks. In 2010–2020, over 96 per cent of all requests submitted by Palestinians for permits to build for purposes of infrastructure, housing, industry or agriculture were rejected.<sup>25</sup> In 2019–2020, the rejection rate increased to over 99 per cent.

40. Although building permits are nearly impossible to obtain, if a structure is built without a permit, as is often the case, it is demolished by the occupying Power. Since the onset of occupation in 1967, the occupying Power has demolished 28,000 Palestinian homes and destroyed vital infrastructure, including water and sanitation facilities.<sup>26</sup>

41. Owners are frequently forced to demolish their own property, at their own expense, to avoid serving time in jail and paying significant financial penalties. In 2021, self-demolition in East Jerusalem increased significantly. Demolition is a traumatic, disempowering experience that uproots communities and scars Palestinian people, particularly children.

42. In 2021, the demolition of Palestinian assets in the West Bank stood at a five-year high; 911 structures were demolished, resulting in the displacement of 1,209 Palestinians.<sup>27</sup> Donor-funded structures were not spared; 140 humanitarian assets, including residential and livelihood structures, funded by the European Union or its member States, were demolished.<sup>28</sup> Many more structures are under constant threat of demolition.

43. In East Jerusalem, the occupying Power has expropriated 57 per cent of land for settlements and public infrastructure and Palestinians are denied access to another 30 per cent of the city. Palestinians are allowed to build on only 13 per cent of the area, much of which is already in use.<sup>29</sup> Such discriminatory zoning restrictions force Palestinians to live in overcrowded enclaves, with obvious consequences for health and well-being.

44. Restrictions, demolition and settler violence create intolerable living conditions that aggravate a coercive environment that pressures Palestinians to leave Area C and creates space for the further expansion of settlements. This creates enduring “facts on the ground”, including through de facto annexation by settlements, that pre-empt the achievement of the two-State solution and the emergence of a viable, contiguous Palestinian state as envisioned by the international community, in line with several resolutions of the United Nations and Security Council.

## F. Mounting suffering in Gaza

45. Since 2007, Gaza has been under complete blockade and has had to deal with the consequences of several military operations that have devastated its infrastructure. In May 2021, Gaza was subjected to the worst military operation since that in 2014. The military operation inflicted serious damage on the already shattered infrastructure, including damage to water, electricity and Internet networks, factories, office buildings, housing units, educational facilities and health-care centres. Meanwhile, investment and the real capital stock declined, and the economy of Gaza experienced technological regression, with total factor productivity contributing little to growth in recent years.<sup>30</sup>

<sup>25</sup> Save the Children, 2021, *Hope Under the Rubble: The Impact of Israel’s Home Demolition Policy on Palestinian Children and Their Families*, London.

<sup>26</sup> Ibid.

<sup>27</sup> See <https://www.ochaopt.org/data/demolition>.

<sup>28</sup> European Union, 2021, One-year report on demolitions and seizures in the West Bank, including East Jerusalem, available at [https://www.eeas.europa.eu/delegations/palestine-occupied-palestinian-territory-west-bank-and-gaza-strip/one-year-report\\_en?s=206](https://www.eeas.europa.eu/delegations/palestine-occupied-palestinian-territory-west-bank-and-gaza-strip/one-year-report_en?s=206).

<sup>29</sup> Ibid.

<sup>30</sup> World Bank, 2021, Economic monitoring report to the Ad Hoc Liaison Committee, November.

46. The destruction of the productive base has entrenched the significant dependence of Gaza on aid, remittances and spending by the United Nations Relief and Works Agency for Palestine Refugees in the Near East and by the Palestinian government. Therefore, fluctuations in these flows strongly impact overall socioeconomic conditions, including the level and depth of poverty. Currently, 80 per cent of the people of Gaza depend on international assistance. The experience in Gaza is a composite of crises of poverty and unemployment, inadequate health care, mobility restrictions, electricity shortages, environmental decline and the enduring psychological impact of a 15-year blockade and prolonged conflicts.

47. To deal with poverty, households in Gaza use various coping mechanisms such as borrowing, selling assets and reducing spending on goods and services or accepting inferior products. Furthermore, the crisis forces children to drop out of school to supplement family income through child labour in various types of work, including in construction, the collection of gravel and demolition.<sup>31</sup>

48. Recovery from the damage inflicted during the most recent military operation requires several hundreds of millions of dollars. Gaza is caught in a perpetual vicious circle, whereby interventions by the Palestinian government, the international community and donors are generally restricted to immediate, urgent humanitarian and rehabilitation needs, with little resources left with which to address structural deficiencies, root causes and long-term development needs. Meanwhile, restrictions on the importation of inputs and technology hinder rehabilitation and recovery efforts.

49. Yet this downward spiral can be reversed. By some estimates, easing a range of restrictions and restoring regular electricity supply and salary payments could boost household purchasing power by 55 per cent, increase exports by 625 per cent, double imports and increase GDP by 39 per cent, and such an upturn in economic activity could reduce unemployment by 23 per cent.<sup>32</sup>

50. Palestinian economic development problems, in Gaza and elsewhere, are fundamentally political in nature. Sustainable recovery in all of the Occupied Palestinian Territory requires ending the restrictions of the dual-use list system on the importation of equipment, inputs and technology, as well as lifting all mobility restrictions and ending the blockade on Gaza, in line with Security Council resolution 1860 (2009). Furthermore, economic revival in the Occupied Palestinian Territory would be accelerated by the economic, administrative and political reunification of Gaza with the West Bank, including East Jerusalem.

## **II. The fiscal crisis deepens**

### **A. Dwindling aid and mounting public debt and arrears**

51. Since 2020, the Palestinian government has been in the grip of one of the deepest fiscal crises in its history. The crisis is characterized by a large financing gap, a precipitous decline in foreign aid and the exhaustion of domestic borrowing sources. Apart from occupation, fiscal management remains the greatest challenge faced by the Palestinian government because of its impact on the ability to carry out basic State functions and meet obligations to pay civil servants, provide essential public goods and services and develop physical and institutional infrastructure. In November 2021, the Palestinian government

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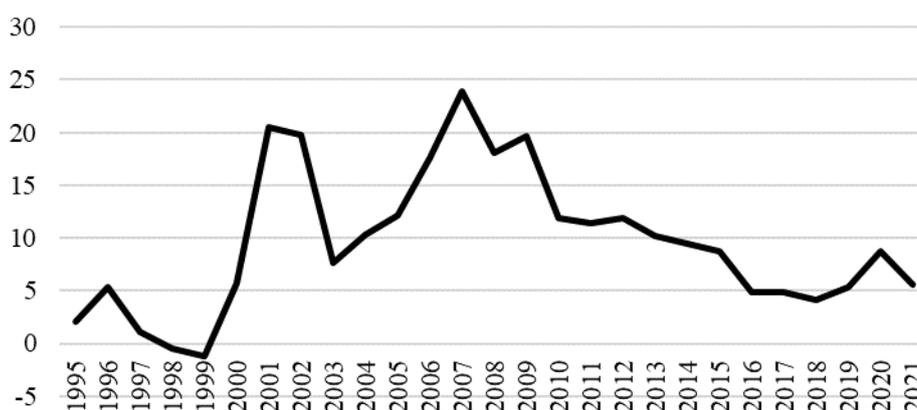
<sup>31</sup> See <https://reliefweb.int/report/occupied-palestinian-territory/acaps-thematic-report-palestine-political-economy-gaza>.

<sup>32</sup> Tony Blair Institute for Global Change, 2018, *Assessing the economic impact of easing measures for the Gaza Strip*, available at <https://institute.global/advisory/assessing-economic-impact-easing-measures-gaza-strip>.

announced that it could pay public servants only 75 per cent of salaries. By mid-June 2022, the Palestinian government was still paying public employees 80 per cent of salaries.<sup>33</sup>

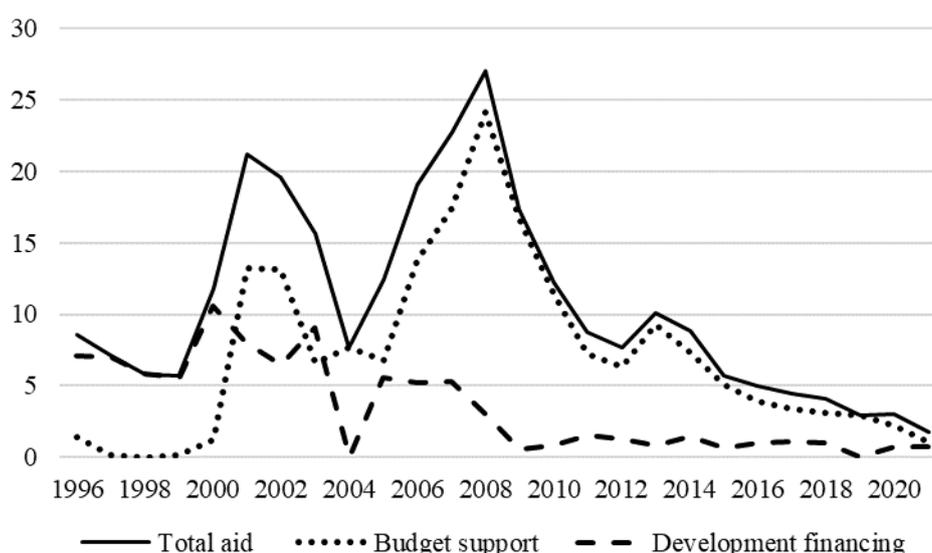
52. The fiscal crisis is mainly caused by the economic consequences of occupation. By the end of the interim period (1994–1999), the Palestinian government was able to balance the budget and most donor support was aimed at funding development (figures 1 and 2). However, following the outbreak of the second intifada in September 2000, the occupying Power implemented mobility restrictions, and the Palestinian economy shrank by 27 per cent in 2000–2002. Consequently, public revenue declined steeply and the government moved from a balanced budget to a recurrent deficit, which reached 21 per cent of GDP in 2002.

Figure 1  
**Recurrent budget deficit as share of gross domestic product**  
(Percentage)



Source: Palestinian Ministry of Finance and Planning.

Figure 2  
**Donor aid as share of gross domestic product**  
(Percentage)



Source: Palestinian Monetary Authority.

<sup>33</sup> Palestinian Ministry of Finance and Planning, 2022, Full-year report 2021: Fiscal development and macroeconomic performance; World Bank, 2022.

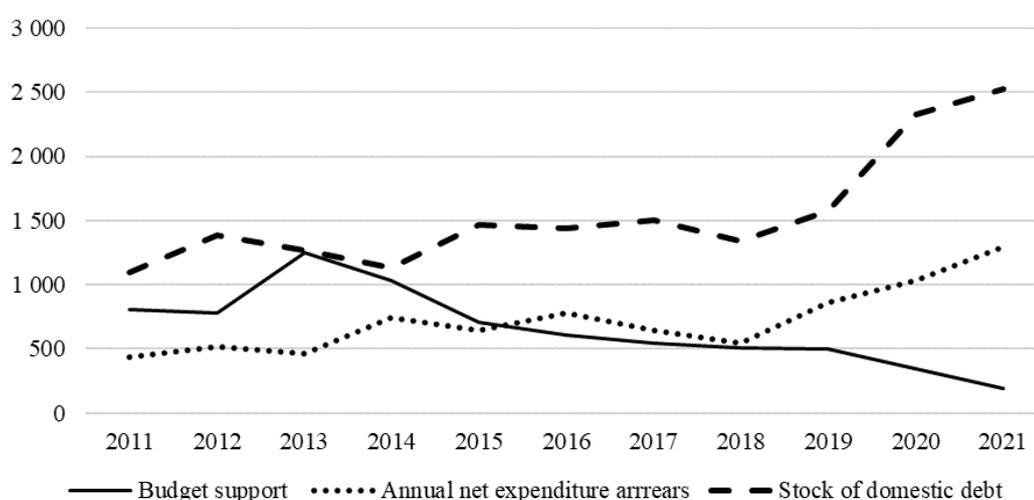
53. In an environment of frequently recurring political, economic and humanitarian crises, the Palestinian government has been implementing far reaching fiscal reforms. By 2021, the government had managed to reduce the recurrent deficit to 5.6 per cent of GDP, from 23.9 per cent in 2007, and raise public revenue to 23 per cent of GDP, from 17 per cent in 2012 and 2013, a favourable ratio by comparative standards. In the same period, the Palestinian government succeeded in reducing the ratio of total expenditure to GDP by 20 percentage points, from 50.5 per cent in 2007 to 30.4 per cent in 2021.

54. Although the deficit may not appear extreme by ordinary standards, it raises significant concerns in the unique Palestinian context in which traditional fiscal sustainability benchmarks do not apply. The Palestinian government does not have a central bank, does not issue a national currency, has little access to international financial markets and has exhausted safe domestic borrowing limits. Other economies can sustain much larger deficits and debt ratios to stimulate the economy or smooth business cycles, yet the Palestinian government lacks the tools and fiscal policy space to do so without adequate donor support.

55. The fiscal horizon has darkened with the decline in aid and the exhaustion of safe domestic borrowing sources. In 2021, total aid fell to \$317 million, or 1.8 per cent of GDP, a steep decline from the \$2 billion, or 27 per cent of GDP, in 2008. Meanwhile, budget support halved compared with in 2020, amounting to \$186 million, or only 1 per cent of GDP, compared with 24 per cent in 2008. In 2007–2018, on average, budget support covered 80 per cent of the recurrent budget deficit but did not cover 54, 25 and 18 per cent of the deficit in 2019, 2020 and 2021, respectively. Meanwhile, development support declined from a peak of 10.6 per cent in 2000 to 0.73 per cent in 2021.

56. With the decline in foreign aid and the leakage of Palestinian fiscal resources to Israel, the Palestinian government was forced to bridge the fiscal gap through a significant increase in borrowing from domestic banks and by accumulating arrears to the domestic private sector and pension fund. By end-2021, overall public debt had reached \$3.8 billion and the arrears stock, about \$3 billion, amounting to a combined 38 per cent of GDP.<sup>34</sup> Meanwhile, domestic debt rose to \$2.53 billion, or 14 per cent of GDP and 23 per cent of total credit, and was over the 15 per cent limit set by the Palestinian Monetary Authority. The previous decade of, simultaneously, a decline in donor budget support on the one hand and mounting stocks of public debt and arrears on the other is shown in figure 3.

Figure 3  
**Fiscal indicators**  
(Millions of dollars)



Source: Palestinian Ministry of Finance and Planning.

<sup>34</sup> Palestinian Ministry of Finance and Planning, 2022.

57. Furthermore, public employee debt to the banking system reached \$1.8 billion, heightening the exposure of the system to the government and its employees, which together account for 40 per cent of total bank credit. The growing stock of public debt and arrears and the high level of exposure of the banking system to the government and its employees elevate the risk of a destabilizing spillover to the rest of the economy by crowding out the private sector and slowing economic activity. For example, the construction sector has been pushed to the limit by debt owed by the public sector.<sup>35</sup> A vicious circle, in which a slowdown in economic activity can aggravate the fiscal crisis by reducing public revenue, should be pre-empted.

## **B. Origins of extreme fiscal vulnerability**

58. Twenty-eight years have passed since the signing of the Paris Protocol, which was aimed at regulating the economic relations between Israel and the Palestinian National Authority for a five-year interim period. Nearly three decades later, the Paris Protocol remains the general framework that governs, constrains and shapes Palestinian macroeconomic, fiscal and trade policies.

59. The asymmetric economic relations established in the Paris Protocol eliminate possibilities for fiscal sustainability by fostering vulnerability and uncertainty. A key feature of the Paris Protocol is the establishment of a revenue clearance mechanism, whereby Israel collects taxes on Palestinian imports from or via Israel and transfers the clearance revenue to the Palestinian government on a monthly basis. This arrangement leaves over two thirds of Palestinian fiscal revenue under the control of the occupying Power, which can (and often does) suspend the transfer of revenue and/or apply unilateral deductions that lack transparency. For example, in July 2018, the Government of Israel enacted a law mandating the deduction from clearance revenue amounts equivalent to the payments made by the Palestinian government to families of Palestinian prisoners in Israel and Palestinians killed in attacks or alleged attacks against Israelis.<sup>36</sup> Such deductions reached \$104 million in 2021.

60. Pioneering research by UNCTAD, since 2011, on the leakage of Palestinian fiscal resources to the treasury of Israel has been cited by international and other organizations, placing the topic on the agenda of negotiations. This resulted in the reimbursement of hundreds of millions of leaked resources to the Palestinian government in 2018 and 2019. However, this leakage has not yet been stemmed. Attempts by Palestinian and international organizations to quantify leakages are non-exhaustive, but all point to the loss of substantial amounts of fiscal resources each year.

61. The complex, multilayered restrictions implemented under occupation stifle economic activity and suppress potential revenue-enhancing GDP gains, thereby entrenching fiscal malaise. The World Bank estimates that greater access by the Palestinian government and Palestinian producers to Area C alone would enhance annual revenue by 6 percentage points of GDP,<sup>37</sup> or \$960 million in 2021, a figure sufficiently high as to eliminate 76 per cent of the fiscal deficit in 2021. Not only does the occupying Power deny Palestinians access to Area C, it also does not abide by the stipulations of the 1995 interim agreement through failure to transfer tax revenue collected in Area C to the Palestinian government. Fiscal resilience and substantiality require removing restrictions, to enable economic growth that will translate into revenue gains and ease pressure on the government to sustain high levels of social spending and act as the employer of last resort.

<sup>35</sup> Portland Trust, 2021, Palestinian Economic Bulletin 181, available at <https://portlandtrust.org/bulletins/palestinian-economic-bulletin-october-2021/>.

<sup>36</sup> TD/B/67/5.

<sup>37</sup> World Bank, 2014, *Area C and the Future of the Palestinian Economy*, Washington, D.C.

62. Stemming the leakage of fiscal resources, allowing Palestinians access to Area C and lifting the blockade on Gaza and other restrictions on productive activities in the West Bank could, in all likelihood, eliminate the entire fiscal deficit and maximize Palestinian fiscal space. This would also bring an end to aid dependence and enable the Palestinian government to realistically pursue achievement of the Sustainable Development Goals, by financing development and investing in rebuilding social, institutional and physical infrastructures, as well as providing essential public goods and social services. Until the Palestinian government can overcome the factors behind fiscal fragility, the international community needs to shoulder its responsibility towards the Palestinian people by extending meaningful and predictable financial support that can sustain the minimum of decent living conditions.

### **C. Path to sustainability and fiscal resilience**

63. Despite a worsening political environment and the decline in donor aid, the Palestinian government continues to pursue fiscal sustainability and articulate development visions, the latest of which is National Development Plan 2021–2023, which emphasizes balanced cluster development based on regional competitive advantages and progressive disengagement from occupation. The aim is social justice and the empowerment of women and youth, as well as openness to global markets, while deepening and widening relations with the Arab region. The Plan recognizes the limits of development under occupation, aiming to leverage economic empowerment for the establishment of a sovereign, independent State rather than exclusively seeking elusive welfare under occupation.<sup>38</sup> The international community should shoulder its responsibility towards the Palestinian people by extending sufficient political and economic support to enable the realization of the admirable goals set out in the Plan.

64. Occupation remains at the root of the chronic Palestinian fiscal crisis and the key obstacle to fiscal sustainability. The pandemic and the decline in donor support have only unmasked a pre-existing condition and exposed the extreme fiscal vulnerability. The optimal path to fiscal sustainability requires ending occupation and empowering the Palestinian government with sovereign control over its borders, access to land and natural resources and the capacity for independent revenue collection. In the meantime, the international community should take measures to ease the perilous fiscal situation by:

(a) Reversing the trend of declining donor aid to ensure that the Palestinian government has the capacity to survive, bridge the recurrent financing gap and increase spending on development and essential social services;

(b) Ensuring that the occupying Power shoulders its responsibilities under international law by lifting all economic restrictions, in line with relevant United Nations and Security Council resolutions. Furthermore, the occupying Power should be encouraged to desist from unilateral deductions from Palestinian clearance revenue and withholding transfers;

(c) Facilitating negotiations for a comprehensive end to the leakage of Palestinian fiscal resources. This entails establishing transparent mechanisms for sharing all relevant trade-related and fiscal data between the Palestinian government and the Government of Israel. The current paper-based clearing system for settling transactions between the two economies needs to be upgraded to an interconnected automated system that allows for the exchange of data in a fast, comprehensive and accurate manner. A recently launched technical cooperation project by UNCTAD aims to contribute to the realization of this objective by strengthening Palestinian customs management capacities and upgrading the UNCTAD Automated System for Customs Data (ASYCUDA) system used by the Palestinian government.

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<sup>38</sup> See <https://andp.unescwa.org/plans/1293>.

### III. UNCTAD assistance to the Palestinian people

#### A. Framework and objectives

65. For over three and a half decades, UNCTAD has been supporting the Palestinian people through policy-oriented research, the implementation of capacity-building and technical cooperation projects, the provision of advisory services and the promotion of international consensus on the needs of the Palestinian people and their economy.

66. The UNCTAD programme of assistance to the Palestinian people responds to paragraph 127 (bb) of the Bridgetown Covenant, which requests UNCTAD to “continue to assess the economic development prospects of the Occupied Palestinian Territory and examine economic costs of the occupation and obstacles to trade and development... with a view to alleviating the adverse economic and social conditions imposed on the Palestinian people”. Furthermore, the United Nations General Assembly, in seven resolutions (69/20, 70/12, 71/20, 72/13, 73/18, 74/10 and 75/20), requests UNCTAD to report to the General Assembly on the economic costs of the Israeli occupation for the Palestinian people.

67. The UNCTAD programme, which aims to build and strengthen the institutional capacities of the Palestinian public and private sectors, addresses the constraints to and emerging needs of the Palestinian economy through the following four clusters:

- (a) Trade and macroeconomic policies and development strategies;
- (b) Trade facilitation and logistics;
- (c) Finance and development;
- (d) Enterprise, investment and competition policy.

#### B. Operational activities under way

68. In response to the above-mentioned resolutions, in 2021, UNCTAD submitted a report to the General Assembly on the economic costs of occupation.<sup>39</sup> An assessment of the economic costs of the restrictions and closure policy imposed following the outbreak of the second intifada in September 2000 was provided, along with estimates of the additional level of poverty caused by restrictions and military operations in terms of the poverty rate and poverty gap at the household level, the minimum cost of eliminating poverty and the potential economic growth that could have been realized if the additional harmful measures and closure policy had not occurred. The report was followed by a more detailed study on occupation policy, arrested development and poverty in the West Bank.<sup>40</sup>

69. In June 2021, UNCTAD conducted a workshop at MAS to present its new integrated simulation framework to Palestinian institutions. Beneficiaries included government institutions, research institutes and academic institutions. As done for previous versions, the updated model was shared with MAS and PCBS, to enable them to forecast prospects for the Palestinian economy and to provide policymakers and the private sector with practical tools with which to evaluate key aspects of the Palestinian economy; assess alternative policy options and scenarios; and assist in formulating economic development strategies in pursuit of the Sustainable Development Goals.

<sup>39</sup> A/76/309.

<sup>40</sup> UNCTAD, 2021, *The Economic Costs of the Israeli Occupation for the Palestinian People: Arrested Development and Poverty in the West Bank* (United Nations publication, Geneva).

70. In early 2022, UNCTAD signed an agreement with the Palestinian Ministry of Finance and Planning on a new round of cooperation in customs management based on ASYCUDA. The project aims, among others, to update the ASYCUDA World system to the most recent release and to provide training to Palestinian customs staff in such areas as customs valuation, risk analysis and post-clearance controls. The goal of the project is to strengthen the fiscal position of the Palestinian government and support its efforts towards trade facilitation and to enhance competitiveness.

71. UNCTAD has been working with the Palestinian Ministry of Finance and Planning on a project to reintroduce the UNCTAD Debt Management and Financial Analysis System to Palestinian institutions. The project aims to enhance the quality and scope of Palestinian public financial management.

### **C. Coordination, resource mobilization and recommendations**

72. In 2021, UNCTAD continued its support to the Palestinian people in coordination with the Palestinian government, international organizations, donors, the United Nations country team and other stakeholders, including civil society. The programme continued to strengthen its ongoing support for the Palestinian people despite adverse and increasingly difficult field conditions.

73. In late 2020, UNCTAD received a grant from the government of Saudi Arabia to sustain the professional capacity required at UNCTAD to fulfil its mandates and support the efforts of the Palestinian people to achieve the Sustainable Development Goals. The grant funds a project that aims to strengthen UNCTAD capacity to examine the economic costs of the occupation and obstacles to trade and development, with a view to alleviating the adverse economic and social conditions imposed on the Palestinian people under occupation.

74. A shortage of extrabudgetary resources continues to limit the ability of UNCTAD to deliver on its mandates and meet the growing need for technical assistance by the Palestinian people and other stakeholders, including civil society and the private sector. Therefore, member States are invited to consider extending resources to enable UNCTAD to fulfil the requests made in the Nairobi Maafikiano and the Bridgetown Covenant and in United Nations resolutions.

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