

PALESTINIAN ECONOMIC BULLETIN

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Main reports

The IMF published a report assessing recent macroeconomic developments in Palestine and providing forecasts

In Q1 2014 Palestinian quarterly GDP decreased by 0.6% in real terms with respect to the previous quarter

In Q1 2014 the current account deficit reached \$418.5m, increasing by 14.6% with respect to the previous quarter and by more than 70% from Q1 2013

Preliminary results of the 2013 annual food security survey show that 33% of Palestinian households are food insecure

Gaza

As the Bulletin went to press, the Israeli military operation launched on 8 July 2014 was ongoing in the Gaza Strip. Alongside the numerous human losses and injuries being suffered during the operation, governmental and international organisations working in Gaza have reported considerable damage to infrastructure and economic loss. The destruction of power, water, health, education and other service facilities poses severe challenges to the already vulnerable economy of Gaza.

Prior to the current operation, Gaza suffered an estimated electricity supply deficit of up to 40% of its total needs.¹ On 30 June, officials at the local power plant had announced they were no longer able to guarantee the provision of electricity for even 8 hours a day.² At the time of going to print, electricity blackouts around Gaza were reported to have reached up to 12 hours per day on average.³ In central Gaza and Khan Younis, reports indicated that cuts lasting approximately 15 hours per day were affecting around 400,000 people. The situation had become more severe following damage to six out of the ten high tension power lines running from Israel into Gaza. As reported by Gisha, this left hundreds of thousands of people completely without power, while hundreds of thousands more were merely receiving between 2-5 hours of electricity per day.⁴

The water supply situation was reported to be equally critical. According to OCHA, damage to water, sanitation and hygiene (WASH) facilities resulted in much lower than normal levels of water being supplied to the population.⁵ As the Bulletin went to print, it was estimated that 1.2 million people had very limited or no access to water or sanitation services due to damage to the electricity system or lack of fuel to run generators to power WASH facilities. At the same time, several areas were reported to be experiencing sewage flooding, which poses public health hazards.

General economic activity was reported to have been virtually paralysed since the beginning of the operation, as most businesses remained closed. At the time of going to press, activity in the crossings in and out of Gaza was reported to be largely limited to the passage of humanitarian aid, emergency assistance goods (including fuel and food), medical evacuations and other exceptional cases. At the same time, while 3,600 fishermen were prevented from reaching the sea, 3,000 herders were in need of animal feed for their livestock, and severe damage to agricultural holdings had been reported - including the partial or total destruction of 58 dunums of green houses and 1,230 dunums of orchards and vegetables. As farmers were unable to access their land, around 2,000 cultivated dunums of irrigated vegetables were at risk of drought and loss.⁶

As hospitals began to run out of essential medicine stocks and more displaced families seek shelter in UNRWA facilities, the UN organisation launched a \$60m emergency appeal to continue its activities in response to the humanitarian crisis during the coming months.⁷

1 www.palthink.org/en/wp-content/uploads/2014/01/Policy-Paper-Electricity-Crisis-in-Gaza.pdf

2 www.maannews.net/eng/ViewDetails.aspx?ID=708897

3 www.gisha.org/updates/3018

4 www.gisha.org/updates/3085

5 www.ochaopt.org/documents/ocha_opt_sitrep_22_07_2014.pdf

6 www.bit.ly/1z6PAM and www.bit.ly/1z70w8

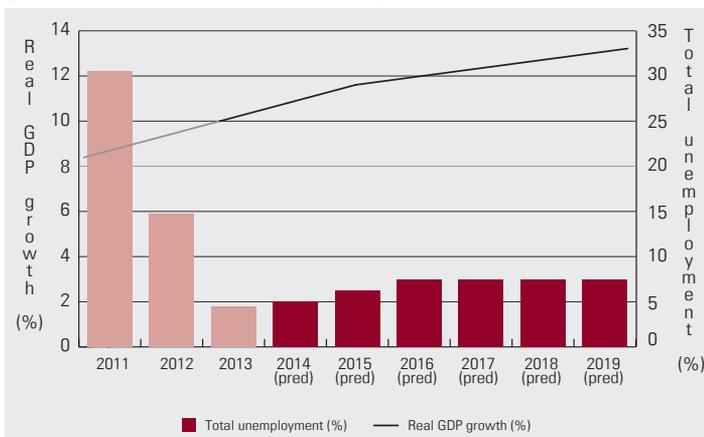
7 www.unrwa.org/sites/default/files/draft_gaza_flash_appeal_loest55.pdf

IMF Report

At the end of June the IMF published a report assessing recent macroeconomic developments in Palestine and providing forecasts.⁸ Experts warn that amid declining growth, rising unemployment and poor social and business indicators, the suspension of peace talks between Palestine and Israel in April further diminished economic recovery prospects. The IMF considers that successful peace negotiations would boost investment by enhancing confidence in the economy, attract donor funds to develop impactful economic programmes and allow for the implementation of private sector-led economic initiatives. Further deterioration on the political front could result in substantially weaker growth prospects, increased unemployment and, potentially, greater social unrest.

The baseline scenario for IMF projections assumes a continuation of political efforts towards internal Palestinian reconciliation; peace negotiations with Israel remaining suspended (although no major steps towards the tightening of current restrictions by Israel is expected); and a continuation of what the organisation characterises as an economic model of large recurrent deficits being financed by unpredictable aid flows under broadly unchanged policies (implying limited reform efforts by the Palestinian National Authority – PNA). Under the status quo scenario the IMF expects country-level real GDP growth to reach a low 2% in 2014, to slightly grow to 2.5% in 2015-2017, and to converge to 3% in the years running through to 2019. These growth rates would imply a decline in GDP per capita in real terms, since they are below historic population growth rates (~3%). Baseline forecasts expect unemployment to further increase from its currently high level by 1-2 percentage points per annum, to reach an all-time high 33% in 2019.

Figure 1: Real GDP Growth and Total Unemployment, Palestine (%), 2011-2013 (Actual) / 2014-2019 (Forecast - Baseline Scenario)



Source: IMF

IMF baseline estimates expect growth in the West Bank to be slower than in the Gaza Strip. Therefore, growth prospects could be revised downward if the recent escalation of violence in Gaza and the resulting socio-

economic deterioration were taken into account. The downside scenario projected by the IMF, assuming the abandonment of efforts to resume peace negotiations (which would upset the political and security status quo), anticipates a major negative impact on the economy, especially if donors signal withdrawal of support.

Therefore, substantial progress on the political front is portrayed as a necessary condition for sustainable economic recovery, although, according to the IMF, this should not be seen as a substitute for much needed economic reform. An upside growth scenario assumes an unlikely final status agreement by the end of 2014, gradual lifting of Israeli restrictions and a 20% increase in FDI and domestic private investment over 2015-2017, a major increase in donor support and profound PNA reforms, which would result in real GDP growth of over 6% in 2015 and of above 10% in the medium term. Under this scenario unemployment would remain high (at 20%+) as a result of high labour force growth and existing labour market frictions and the assumption that there is no net increase in employment of Palestinian workers in Israel.

Finally, although the IMF praises recent PNA efforts on the fiscal front (including a reduction of the fiscal deficit in 2013), it also highlights that the government could do more even under the current circumstances to help expand the role of the private sector in the economy by strengthening the business climate. Recommended measures include the reduction of the cost of doing business, the completion of a competition framework, the establishment of adequate regulatory bodies, the simplification of burdensome procedures and the update of economic legislation. It is also recommended that the PNA focuses on capacity building to effectively absorb scaled up donor aid in the event of a breakthrough in peace negotiations.

National Accounts Q1 2014

Data recently published by the Palestinian Central Bureau of Statistics (PCBS) suggest that in Q1 2014 country-level quarterly GDP decreased by 0.6% in real terms with respect to the previous quarter, but was 7.1% higher than in Q1 2013.⁹ In Q1 2014 quarterly real GDP per capita in Palestine was 1.4% lower than in Q1 2013 (-0.6% in the West Bank and -3.5% in Gaza).

The year-to-year quarterly GDP growth was fully explained by the economic activity in the West Bank, while Gaza registered a real GDP drop of 1.1%. The latter was mainly explained by a decrease of almost 70% in the value added by construction activities in Gaza, where the sector's contribution to GDP fell from almost 15% in Q1 2013 to less than 5% in Q1 2014.

The observed yearly growth is inconsistent with recent trends and available forecasts. Although the PCBS confirmed the accuracy of the preliminary computations, it might be possible that the reported growth figures are

8 www.imf.org/external/country/WBG/RR/2014/063014.pdf

9 www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_NA-Q1-2014e.pdf

reflecting seasonal behaviours in a number of sectors and/or are related to accounting techniques subject to adjustments in subsequent revisions. In particular, this is suggested by the contrast between poor growth/decline in most sectors together with an extraordinary increase in wholesale, retail and services activities (Table 1).

Table 1: Value Added by Economic Activity and Sectorial Contribution to GDP, Palestine, Q1 2013/2014

| Economic Activity | Value Added (Constant 2010 USD Millions) | | | % Contribution to GDP | |
|--|--|---------|----------|--------------------------|---------|
| | Q1 2013 | Q1 2014 | % change | Q1 2013 | Q1 2014 |
| Agriculture, Forestry and Fishing | 96.2 | 97.1 | 0.9% | 3.4 | 3.2 |
| Mining, Manufacturing, Elec. and Water | 443.3 | 431.5 | -2.7% | 15.8 | 14.3 |
| Construction | 312.4 | 271.1 | -13.2% | 11.1 | 9 |
| Wholesale, Retail Trade, others | 488.1 | 635.5 | 30.2% | 17.3 | 21.1 |
| Transportation and Storage | 56.3 | 61.6 | 9.4% | 2 | 2 |
| Financial and Insurance Activities | 101 | 102.1 | 1.1% | 3.6 | 3.4 |
| Information and Communication | 152.3 | 149.5 | -1.8% | 5.4 | 5 |
| Services | 538.8 | 591.4 | 9.8% | 19.1 | 19.6 |
| Public Administration and Defense | 354.8 | 344.6 | -2.9% | 12.6 | 11.4 |

Source: PCBS

Balance of Payments and External Trade

In Q1 2014 the current account deficit reached \$418.5m, increasing by 14.6% with respect to the previous quarter and by more than 70% from Q1 2013.¹⁰ The deficit represents around 11% of quarterly GDP at current prices. This year-to-year quarterly variation was mainly explained by an increase in the trade balance of goods deficit and a decline in the balance of current transfers. Donor current transfers represented more than 35% of the total value of receipts from abroad in Q1 2014. The surplus in income balance (\$411.2m) partially offset the overall current account drop, rising by more than 40% between Q1 2013 and Q1 2014. The sharp rise in the income balance derives from increases in both compensation of employees working in Israel (\$366.5m in Q1 2014) and investments income (\$35.9m in Q1 2014, mostly explained by the interest received on Palestinian deposits in banks abroad).

Table 2: Q1 and Q4 2013, Q1 2014 Balance of Payments

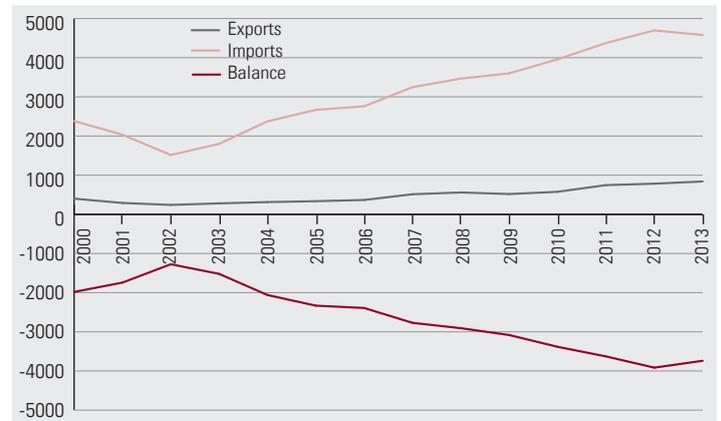
| Item | Q1 2014 (USD millions) | Q4 2013 (USD millions) | Q1 2013 (USD millions) | Change (%) (Q4 2013-Q1 2014) | Change (%) (Q1 2014-Q1 2013) |
|--|------------------------------|------------------------------|------------------------------|------------------------------------|------------------------------------|
| Current Account | -418.50 | -365.30 | -240.20 | 14.6% | 74.2% |
| Trade Balance of Goods (deficit) | -1,293.10 | -1,125.70 | -1,106.10 | 14.9% | 16.9% |
| Trade Balance of Services (deficit) | -94.80 | -139.10 | -97.10 | -31.8% | -2.4% |
| Income Balance | 411.20 | 361.40 | 292.90 | 13.8% | 40.4% |
| Balance of Current Transfers | 558.20 | 538.10 | 670.10 | 3.7% | -16.7% |
| Capital and Financial Account | 355.40 | 479.50 | 191.90 | -25.9% | 85.2% |
| Net Capital Account | 80.00 | 87.00 | 144.20 | -8.0% | -44.5% |
| Net Financial Account | 275.40 | 392.50 | 47.70 | -29.8% | 477.4% |

Source: PCBS and PMA

The deterioration in the Palestinian trade balance of goods during Q1 2014 is part of a long term trend. Although it experienced a slight decline in 2013, annual external

trade deficit has been on the rise since 2000 (Figure 2) and Palestinian trade remains heavily dependent on Israel. Much needed diversification and sustainability of Palestinian exports requires a broad relaxation of Israeli-imposed restrictions on movement as a necessary condition.

Figure 2: Annual Exports, Imports and Net Trade Deficit in Goods, Palestine, 2000-2013 (USD thousands)



Source: PCBS

More recently, while Palestinian exports increased by 6.3% in May 2014 with respect to May 2013, imports rose by almost 16% over the same period.¹¹ As a result, the trade deficit in May 2014 amounted to \$382.7m, increasing by 18% from May 2013.

Food Insecurity

Preliminary results of the 2013 annual food security survey, conducted by the PCBS, UN agencies and other international organisations, show that 33% of Palestinian households are food insecure.¹² This means that approximately 1.6m Palestinians (roughly 40% of the total population) fail to access sufficient, safe, nutritious food to maintain a healthy and active life.¹³

The survey classifies households into four groups according to their level of access to food: food insecure, vulnerable to food insecurity, marginally food insecure and food secure. Cross-group transition takes place following increases in household monthly income and/or monthly consumption (both measured in adult equivalent per day values).¹⁴ In 2013 the percentage of households classified as insecure and vulnerable remained almost the same as in 2012, reversing a positive trend of continuous improvement in food insecurity between 2009 (36%) and 2011 (27%). However, the proportion of food secure households increased by 11 percentage points in 2013, marking a significant improvement in the transition towards food security by households which were marginally food insecure in 2012.

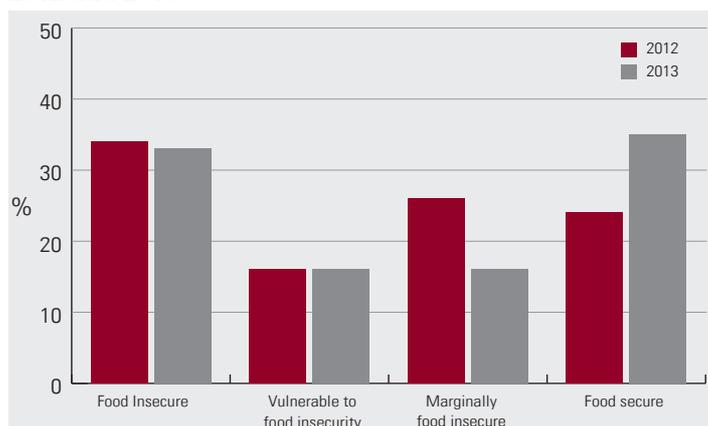
11 www.pcbs.gov.ps/site/512/default.aspx?tabID=512&lang=en&ItemID=1172&mid=3171&wversion=Staging

12 www.pcbs.gov.ps/site/512/default.aspx?tabID=512&lang=en&ItemID=1135&mid=3171&wversion=Staging

13 www.who.int/trade/glossary/story028/en/

14 www.apis.ps/up/1393744149.pdf

Figure 3: Household Food Security Levels in Palestine, 2012 and 2013



Source: PCBS, FAO, UNRWA and WFP

In 2013 the prevalence of food insecurity in Gaza (57%) was much higher than in the West Bank (19%). The challenging conditions derived from the long term restrictions imposed on Gaza by the government of Israel have led to structural economic stagnation and a continuous deterioration of the living standards. As reported by UNRWA, the number of Palestinian refugees relying on food aid has increased from less than 80,000 in 2000 to over 830,000 today. The grave humanitarian consequences following the recent escalation in Gaza are likely to further deteriorate food security standards and have long-lasting impact on its population.

Entrepreneurship

The fourth Startup Weekend Gaza (SWG) took place on 19-21 June.¹⁵ Despite the relatively small start-up scene in Gaza, 150 companies were selected to participate in the hands-on web and mobile technology event from among 650 applicants, marking the largest-to-date event of its kind in Gaza.¹⁶ As such, SWG demonstrates the existence of a young, vibrant community committed to working for a better living through innovation and creative thinking.

In Gaza, women and youth are taking the lead in the entrepreneurship scene. This phenomenon could result in tangible improvements for such marginalised population segments if conditions for the sustainable development of the sector are promoted. More than half of SWG participants were female and the youngest participants were 14 and 16 years old.

¹⁵ www.gaza.startupweekend.org/

¹⁶ www.wamda.com/2014/06/startup-weekend-gaza-4-turning-point-ecosystem

During the event participants were supported by almost 30 local and international coaches, and 71 start-ups pitched their business ideas to a panel of judges. The best 25, two-thirds of which were presented by women, were selected to receive further assistance in developing their ideas during the event. On the final day the three top projects were chosen to participate in incubating programmes. The winner, who was also granted a workspace, mentorship and monetary support, was Lilac for Innovation Design, a platform for virtual interior design modelling created by 26-year-old Hala Eid Naji.¹⁷ The runner up, Fun Lab (a virtual platform for teaching chemistry, biology, physics and computer science to young students), is a project led by the youngest participant in the competition, 14-year-old Eyas Syam. Eyas said that his victory "...means a lot for Gaza because my project will help other kids at school, and get others to start working on similar startups that can make their lives easier", adding that for him SWG has been "...the first step in [his] entrepreneurial life".¹⁸ Additional prizes were awarded to the best female team and the top business-to-business project.

NBC Award

In June the National Beverage Company (NBC), the Palestinian producer of Coca Cola and Cappy drinks, received an award from Coca Cola for sustainability and community empowerment. This was the second time the NBC received such a distinction, after being awarded the same prize in 2012. The NBC was chosen from 96 Coca Cola bottling companies operating in Eurasia and Africa, at a ceremony in Istanbul.¹⁹ The Palestinian company, established in Ramallah in 1998, has three plants and operates through four branches in the West Bank and Gaza.

PEX June Trading

In June the AI-Quds index continued its downward trend and decreased by 3.9% from the previous month. The index reached its highest (527.77 points) and lowest (502.81) levels on 8 June and 30 June (the last day of trading), respectively. A total of 15.6m shares worth \$25.5m were traded in 22 sessions. Market capitalisation was \$3.1bn.

¹⁷ www.facebook.com/LilacForDesign

¹⁸ www.barakabits.com/2014/06/winners-took-home-swgaza-decide-going-build-lives

¹⁹ www.english.wafa.ps/index.php?action=detail&id=25666

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