Bulletin Special Feature
December 2014

The Portland Trust

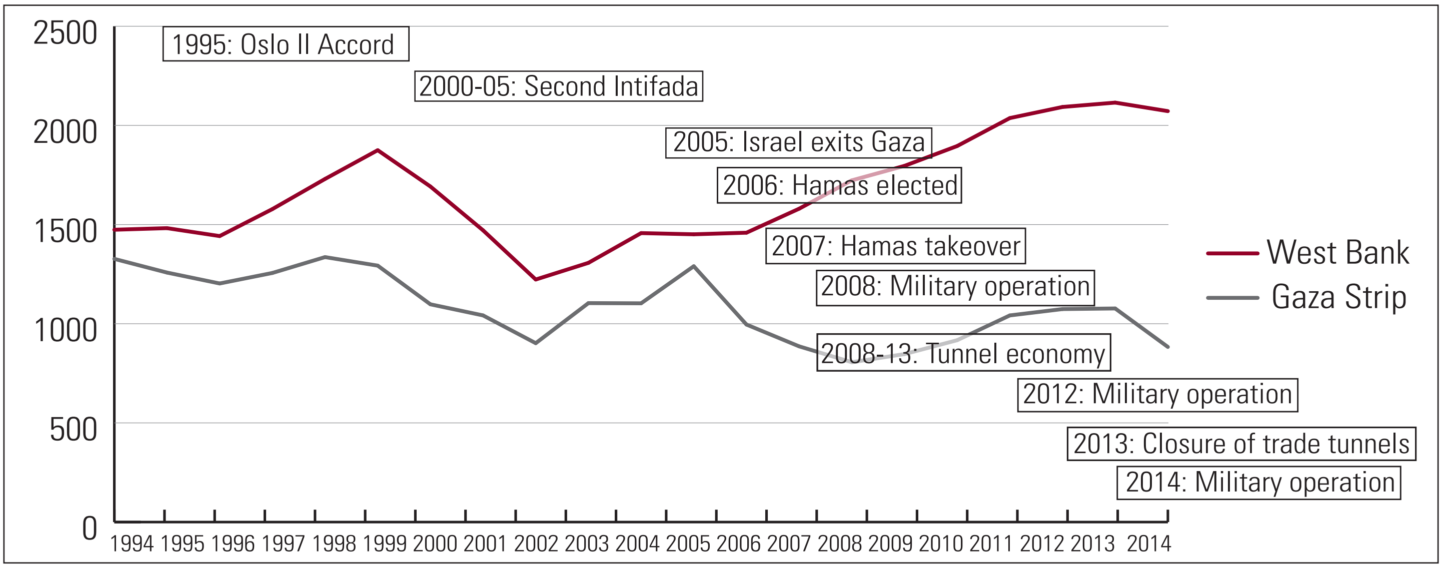
# Gaza's Reconstruction

*This month the Bulletin takes an in-depth look at the historical, current and prospective state of Gaza's economy. In the aftermath of the most recent military operation this summer, key stakeholders share their views on the way forward for sustainable recovery, reconstruction and growth. This report builds on three previous special features (2007, 2010 and 2012) which examined the effects on Gaza's private sector in the wake of multiple political and military shocks.*

## Gaza: 20 years of instability post-Oslo

Gaza's economy has been characterised by extreme volatility over the last 20 years, with a cyclical pattern of destruction of economic value (driven by political and security related events) followed by periods of short-term recovery.[1] Following the signing of the Oslo Accords and the establishment of the Palestinian National Authority (PNA) in 1994, Gaza's economy moved onto a positive growth trajectory and by the late 1990s per capita GDP was on the rise (Figure 1). However, the onset of the Second Intifada in 2000 led to a severe contraction in economic activity, with per capita income falling sharply through to 2002. The period 2003-2005 saw a resumption of positive growth in Gaza, with economic performance exceeding that of the West Bank – by the end of 2005 per capita GDP had nearly recovered to late 1990s levels. Since then, however, a succession of political upheavals and military operations in Gaza have set the economy on a divergent growth path from the relatively more stable economy of the West Bank. Sustained internal divisions and violence between Palestinian factions had significant negative effects on the economy in 2006 and 2007, culminating in Hamas's takeover in 2007. This was followed by the intensification of restrictions on the movement of people and goods in and out of Gaza by the Government of Israel, marking the onset of a period of increased economic isolation. Gaza's economy entered a period of recovery from 2009, driven by both donor-supported reconstruction efforts after the 2008 Israeli military operation and increased private sector activity. The latter was aided by increased trade following the construction of tunnels under the border between Egypt and Gaza. A new military operation in 2012 and the closure of the trade tunnels by the Egyptian government in 2013 left the economy in a fragile state – with the latter suffocating private sector activity and leading to reduced access to vital commodities.[2] Most recently, Gaza's economy suffered a new shock following extensive damage derived from the war in the summer of 2014.[3]

**Figure 1: Real GDP per Capita (2004 USD), Gaza Strip and West Bank, 1994-2014**




*Source: PCBS (1994-2013) / IMF (2014 forecast)*

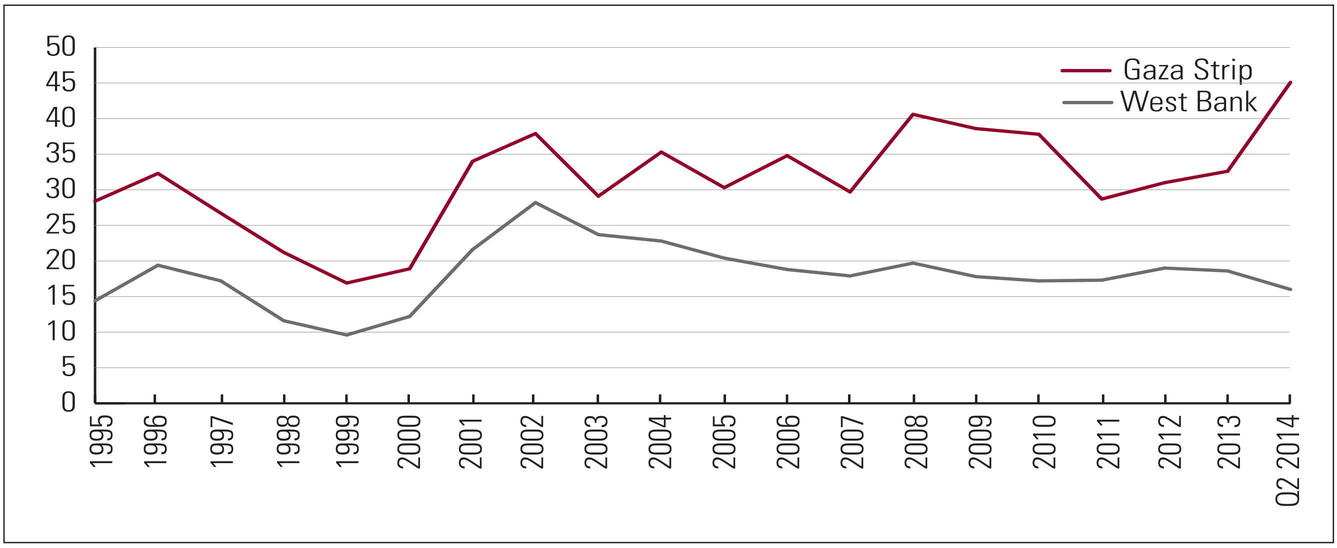
1 Unless explicitly referenced the text refers to Gaza's economy and not the combined Palestinian economy.
2 http://documents.wfp.org/stellent/groups/public/documents/ena/wfp262728.pdf
3 See Bulletin 97.

## Long-lasting effects

Two decades of volatility and increased economic isolation have seen Gaza's contribution to overall Palestinian GDP drop from almost 36% in 1994 to around 24% in 2013. By the end of 2014, Gaza's real GDP per capita is expected to be 33% lower than in 1994 (IMF), with the West Bank growing by more than 40% over the same period.[4] Other economies in the region have registered much higher income per capita growth over the same period, including Egypt (69%) and Jordan (56%).

Poor economic performance has also heavily impacted Gaza´s labour market. Total unemployment reached 45.1% in Q2 2014, almost triple the 16.9% registered in 1999 before the onset of the Second Intifada. It is expected that labour market indicators will deteriorate further as data for the second half of the year becomes available. With 21.8% of Gaza´s population aged 15-24 and youth unemployment reaching almost 70% in Q2 2014, there is an urgent need to create sustainable jobs to avoid a total collapse of the labour market over the coming years.

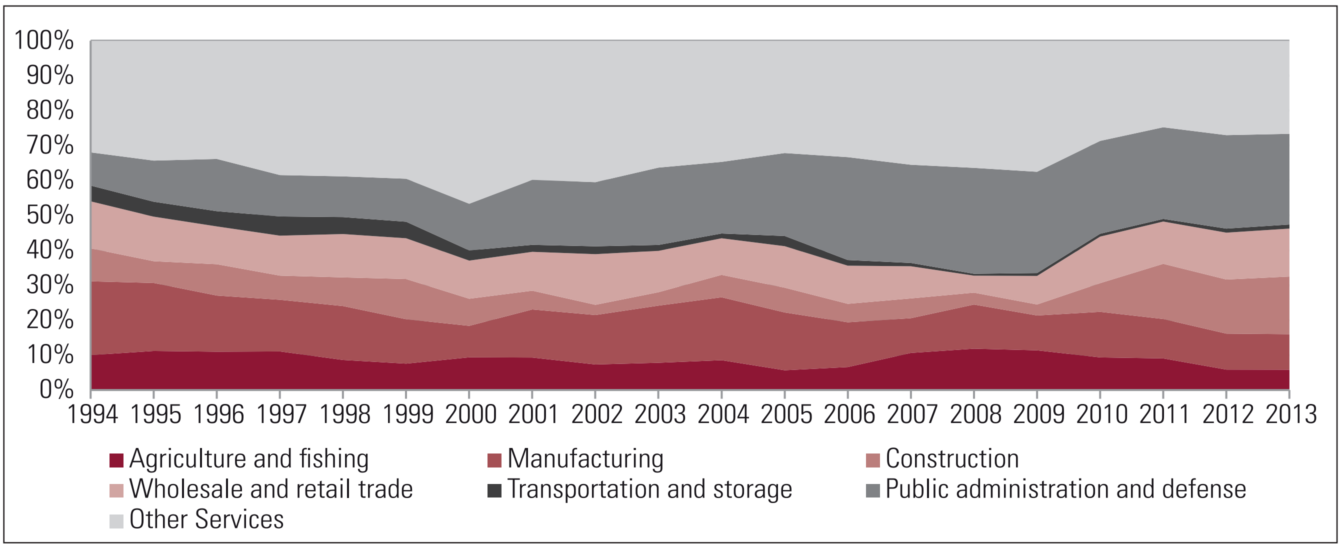
**Figure 2: Total Unemployment (%), Gaza Strip and West Bank,1995-2014**




*Source: PCBS*

Political and economic instability has also fundamentally altered the structure of Gaza's economy. Traditionally strong sectors such as manufacturing and agriculture have seen their share in GDP decline from 21% and 10% in 1994 to just 10% and 6% in 2013, respectively. This can be explained in part by the collapse of exports in the wake of the restrictions on the movement of goods and people. The decline in tradable sectors corresponds almost exactly to a substantial growth in public administration and defence, which saw its share of total output rise from 9.5% in 1994 to 25.6% in 2013 (Figure 3). Construction has also gained heightened importance in recent years in the wake of repeated destruction and subsequent reconstruction efforts. However, the sector's performance has also been volatile, being heavily correlated to restrictions on the import of construction materials into Gaza.

**Figure 3: Sectorial Breakdown of GDP (%), Gaza Strip, 1994-2013**




*Source: PCBS*

4 www.imf.org/external/country/WBG/RR/2014/091214.pdf

## Looking forward: recovery, reconstruction and beyond

The military operation in Gaza in the summer of 2014 marks yet another profound shock in its history of economic volatility. Following severe contraction in economic activity during the war, partial recovery is expected in 2015 as a result of the reconstruction efforts announced at the Cairo donor conference in October 2014. However, in the light of past post-conflict experiences, the main challenge lies in ensuring that the effects of reconstruction are not short-lived. While short-term relief will continue to be vital in the coming weeks and months, longer-term efforts must focus on creating the conditions necessary for a viable, sustainable economy, with a vibrant private sector at its heart.

The PNA's National Early Recovery and Reconstruction Plan for Gaza, produced in advance of the Cairo conference, defines the vision for Gaza as one of "*…sustainability and self-sufficiency, where Gaza is an integral driver of a growing Palestinian economy, united with the West Bank and opened up to the rest of the world.*"[5] The government also expects business to play a key role in the recovery and reconstruction efforts and is committed to providing a "*proper enabling environment for the private sector to work efficiently.*" In particular, the Government wishes to *"leverage the private sector via Public Private Partnerships*", including in several 'keystone' infrastructure projects. With a long-standing infrastructure deficit and extensive damage to utilities during the last war it is an absolute priority to improve the provision of power, water and sanitation facilities in Gaza.

On top of the critical need to improve basic infrastructure, the PNA notes that sustainable private sector development "*cannot be achieved without ensuring the removal of the blockade and access and movement restrictions, allowing for normal trade between Gaza and the West Bank, neighbouring countries, and world markets."* At the same time, strong governance and political stability in Gaza are also pre-conditions for the implementation of the recovery plan and for stimulating private investment. The PNA plan recognises these requirements, stating that "*the National Consensus Government will seize the opportunity presented by its recent formation to harmonize and integrate the previously divided government structures (…), maintaining and expanding [its] operational capacity."* Despite internal reconciliation efforts, ensuring political unity and stability remains a major challenge for the Consensus Government.

Robert Serry, the UN Special Coordinator for the Middle East Peace Process, echoed the PNA's sentiments at the UN Security Council in September 2014, claiming that *"Gaza must now be opened up for reconstruction and recovery"*, whilst also acknowledging the need to address "*legitimate security concerns regarding 'dual-use' materials"*.[6] As a result, the UN designed and launched a trilateral agreement, including the PNA and Israel, to monitor the entry of dual-use construction materials into Gaza with the objective of ensuring that they do not get diverted for other purposes. The implementation of the needed mechanism implies both heavy costs and additional logistic arrangements, and has proved challenging during the first weeks following its announcement. Towards the end of November 2014, a further agreement to allow for the passage of materials to rebuild thousands of homes was announced, and is expected to be the starting point for a smoother, sustainable recovery in the construction sector.[7]

## Other stakeholders' views

For this Bulletin, a number of leading stakeholders in the Palestinian private sector and academic community were interviewed, to understand their views on Gaza's reconstruction. While they all recognise economic opportunities moving forwards, a need for a definitive change in the political front is widely acknowledged as a necessary condition for sustainable development.

The economist Omar Shaban, founder and director of the Gaza-based think tank PalThink for Strategic Studies, criticised the PNA plan for what he regards as 'bottom up' planning without specific development goals, lack of adequate participation of business and civil society in its development, and an absence of clear criteria for measuring macroeconomic impact and progress. Mr Shaban told the Bulletin that while current efforts for reconstruction should be welcomed, they need to be placed within a longer-term strategic vision for Gaza's development. He also added that "*…the current pace of progress in reconstruction activities is too slow. The process must be accelerated not just to improve living conditions for the people in Gaza, but also to prevent the resumption of violence.*"

Looking to the future Mr Shaban said: "*…with unemployment already at unsustainably high levels and thousands of new labour market entrants every year (including some 20,000 graduates), job creation is an absolute priority. The coalition government, while a necessary political development, will need to absorb current Hamas employees into its*

5 www.bit.ly/1Dk42py
6 www.bit.ly/1zgnXp6
7 www.bit.ly/1uJhaxE. A further announcement was made by Mr Serry on 11 December (see Bulletin 99 and www.bit.ly/1svNJVH).

*payroll. If this happens, the PNA will not be able to absorb any new workers for a decade, leaving the private sector as the only part of the economy capable of creating jobs in the coming years*." Beyond job creation, Mr Shaban sees the private sector playing a vital role in facilitating reconstruction through service delivery and domestic investment, and particularly by leveraging expertise and capital from the Palestinian diaspora. "*The private sector can bring prosperity and change the landscape in Gaza. For this, it is essential to harness business creativity and innovation by involving the private sector in decision-making around future planning in Gaza*", he concluded.

Dr Nabeel Kassis Director General of the Palestine Economic Policy Research Institute (MAS), believes that Gaza has great potential for development: "*Gaza, along with other Palestinian regions, needs to be given the opportunity to build on its comparative advantages and to become competitive in specific economic activities, by leveraging its young, educated and vibrant human resource base"*, he said. Dr Kassis stressed that such potential can only be untapped within a context of national political and economic unity and through broad engagement of the public and private sectors and civil society. However, he concluded that a drastic change in the political situation is still the main pre-requisite for economic development, considering that "*we simply cannot put the economic cart before the political horse.*"

The private sector must take the lead in driving Gaza's reconstruction according to Samir Hulileh, CEO of PADICO Holdings: *"With the government failing to function properly, there is a lack of a real reconstruction process in Gaza. Private sector firms should not wait for donors' money, which may not come, or government actions, which may be delayed. Instead, with the economy slowing down dramatically, business has a vital role to play in leading Gaza's reconstruction through investment."* Mr Hulileh thinks that companies must get back to business as soon as possible, *"Factories need to be re-built and resume production as soon as possible; farmers need to access and farm their land. Within their capacity, efforts by private investors can add value and create much-needed employment opportunities for the people of Gaza."*

For his part local business leader Jawdat Al-Khoudary pointed out the urgent need to improve the provision of private services as a critical enabler for business and sustainability. In this sense Mr Al-Khoudary said: "*In the past Gaza was a sustainable, thriving economy open for trade with the region. In order for Gaza to regain this position immediate solutions are needed in essential sectors such as energy, water and solid waste. Once this is achieved efforts should be directed towards regaining the stature of Gaza as an economic engine for the rest of the country.*"

## A bigger vision

Two decades of instability have resulted in a pattern of declining GDP per capita, high unemployment and continued deterioration of Gaza's historically strong productive sectors. In the aftermath of the latest war, and as early recovery is underway, it is encouraging to see the objectives of the government, business and academia directed towards the development of a bolder, long-term vision for Gaza with the private sector at its heart. However, the extent to which such a vision can be translated into concrete action will depend on a wide range of factors. While a definitive political solution is a pre-requisite for any real progress, current early recovery and reconstruction efforts could be a first step by public, international and private sector actors towards long term development and economic sustainability.

In this context, creating a vision for an open, stable, connected and thriving Gaza can help guide shorter-term interventions to improve the living conditions on the ground. Both are essential to create hope and showcase the potential of Gaza and its people. Breaking the cycle of conflict recurrence is as essential as laying the foundations for a new development paradigm in Gaza.

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