

## THE 100<sup>th</sup> ISSUE OF THE BULLETIN

### The Portland Trust celebrates the 100th issue of the Palestinian Economic Bulletin

The Portland Trust, in collaboration with the Palestine Economic Policy Research Institute (MAS), published the first edition of the 'Palestinian Economic Bulletin' in October 2006. In the intervening years we have sought to provide accurate insights into the Palestinian economy to our local and global readership. This month I am proud to introduce our 100th issue.

I would like to express gratitude to all those who have contributed to the Bulletin over the years. In particular, I would like to thank our partners at MAS for their work and support each month. Without them the Bulletin would not be possible. At the same time, it would be remiss not to acknowledge our readers, not just for reading the Bulletin each month but also for their constructive feedback.

As I write, we are at a time of political uncertainty and economic slowdown following the collapse of the peace negotiations in April 2014 and the war in Gaza last summer. Preliminary estimates indicate that the Palestinian economy shrunk by 2.5% in 2014, with the war intensifying a declining trend observed since 2012 after five years of economic improvement previously. GDP per capita has only increased marginally over the last two decades and is estimated to have fallen by 5.5% in 2014. In Gaza, GDP per capita has declined by 33% since 1994. Total unemployment is estimated at 27%, with unemployment rates of youth aged 20-24 in the West Bank and Gaza of 27.5% and 68.3%, respectively.

The Portland Trust continues to believe that a vibrant private sector-led economy is crucial for sustainable growth and job creation, as well as for peace in the region to take hold. During 2014 we have, therefore, sustained our efforts to support the development of Palestinian businesses through the implementation of 'Beyond Aid', an economic initiative by the Palestinian private sector which envisages the creation of almost 400,000 jobs by 2030.<sup>1</sup>

However, it must be acknowledged that any private sector development efforts will be seriously constrained without an improvement to the enabling environment and, in particular, political progress leading to the creation of a thriving Palestinian state. It is therefore absolutely crucial that all concerned parties work together towards achieving a definitive political settlement alongside the creation of a thriving economy, which, in turn, will reinforce meaningful peace efforts.

We hope that the Palestinian Economic Bulletin will continue to inform the public debate and inspire business, policy makers and international organisations to direct their efforts towards the creation of a sustainable economy.

**Sir Ronald Cohen**  
Chairman, The Portland Trust

### Dr. Nabeel Kassis, MAS Director General

MAS perceives its partnership with The Portland Trust as one of high value that enables us to reach out to a significant number of interested local and international readers and inform them of the major developments in the Palestinian economy. For MAS, the Palestinian Economic Bulletin is a vital instrument for dispersing knowledge about the Palestinian economy domestically, regionally, and internationally. The constantly growing readership is a testimony of the success of this endeavour. Through its nearly decade-long history (since 2006) and its 100 issues, the Bulletin has recorded moments of impressive growth as well as disappointing stagnation and even declines in the economy. Last year was a challenging one for all, especially the second half following the devastating effects of the war in the summer in Gaza. We start 2015 with the hope that there will be more positive news for the Bulletin to write about in the coming months.

<sup>1</sup> [www.portlandtrust.org/publications/beyond-aid-palestinian-private-sector-initiative-investment-growth-and-employment](http://www.portlandtrust.org/publications/beyond-aid-palestinian-private-sector-initiative-investment-growth-and-employment)

## PALESTINIAN ECONOMIC BULLETIN

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### Main reports

*Israel has not transferred tax revenues worth around \$125m to the PNA, resulting in delayed payment of December salaries to civil servants*

*42,000 individuals have submitted damage assessments through the trilateral Gaza Reconstruction Mechanism, with 15,602 accessing construction materials*

*An international tender for oil exploration in the Rantis-1 block in the West Bank was re-launched*

*In Q3 2014 the current account deficit reached 8.1% of quarterly GDP at current prices, a substantial decline from the previous quarter*

*In Q3 2014 Palestine's International Investment Position (defined as external assets minus foreign liabilities) stood at \$1,171m, marking a 19.5% increase from Q2 2014*

*2014 saw the Al-Quds index fall by 5.5%, closing for the year at 511.77 points*

### Economic Forecasts for 2015

The Palestine Monetary Authority (PMA) released a report reviewing the performance of the Palestinian economy during 2014 and providing forecasts for 2015.<sup>1</sup> Following a period of economic slowdown between 2011-2013, preliminary estimates show the economy entering into a period of actual contraction in 2014. Despite an improvement witnessed during the first half of 2014, driven primarily by the performance of the West Bank, estimates for the second half of the year are for a sharp deterioration in the wake of a slowdown in economic activity following the Gaza war. The PMA projects a 2.7% fall in the real GDP growth rate for 2014 (compared to growth of 2.2% in 2013) and 5.5% reduction in GDP per capita (compared to a decline of 0.8% in 2013). Unemployment is expected to rise to 29% (23.4% in 2013). These figures compare to the most recent Palestinian Central Bureau of Statistics (PCBS) estimates of falls in real GDP and real GDP per capita of 2.5% and 5.4% respectively, and an unemployment rate of 26.7%.<sup>2</sup>

The PMA acknowledges that the forecasts are sensitive to the conditions of economic and political stability, particularly given that the Palestinian economy operates within a high-risk environment. In this context, the report analyses the potential shocks, both positive and negative, which may impact the key economic indicators.

Table 1 shows past data and estimates for real GDP growth and unemployment in Palestine in 2015. The 'base' case assumes that there will be no significant change in the political or security conditions observed in 2014. Other key variables include stable levels of donor support to the Palestinian National Authority's (PNA) budget and no variations in the clearance revenues transferred to the PNA by the Government of Israel (GoI). It is also assumed that the PNA will continue to pursue the objective of decreasing its budget deficit through increases in income tax and VAT collection and the continuation of the freeze in net hiring of public employees. Under this scenario, restrictions on movement and access imposed by the GoI are also assumed to remain unaltered, with similar numbers of Palestinian workers in Israel. Under this scenario real GDP is expected to grow by 2.9% in 2015, with a marginal increase in GDP per capita growth and unemployment dropping by 2 percentage points to 27%. The baseline estimates for 2015 also predict that total consumption, total investment and the trade deficit will increase by 6.8%, 15.5% and 22.3%, respectively.<sup>3</sup>

**Table 1: Economic Forecasts**

	2011	2012	2013	2014 (est)	2015 (Forecast)		
					Base	Optimistic	Pessimistic
GDP growth (%)	12.4%	6.3%	2.2%	-2.7%	2.9%	8.1%	-3.9%
GDP per capita growth (%)	9.1%	3.1%	-0.8%	-5.5%	0.2%	5.0%	-6.7%
Total unemployment (%)	20.9%	23.0%	23.4%	29.0%	27.0%	23.0%	31.0%

Source: PMA

1 [bit.ly/1wdx4Be](http://bit.ly/1wdx4Be)

2 <http://bit.ly/1zrhjx0>. Both organisations use separate forecasting models, which explains discrepancies between their results

3 Interestingly, the PCBS forecasts smaller fluctuations in the trade deficit under all three scenarios

The 'optimistic' scenario assumes that major advances take place in the political sphere, with internal reconciliation between competing factions in the West Bank and Gaza, security conditions improving and peace talks resuming. It also assumes inflows of funds for the reconstruction of Gaza and a reduction of restrictions on the movement of people and goods to the Strip. It further envisages increased numbers of Palestinian workers in Israel and enhanced donor aid inflows for budget support and development expenditure. Such conditions are more conducive to successful economic performance in 2015, and are forecast to lead to real GDP growth of 8.1%, real GDP per capita growth of 5% and a 6 percentage point fall in the unemployment rate to 23%. Consumption would increase by 15.7% and total investment by 26.4%. However, Palestine's large structural trade deficit would increase substantially by 42.1% – while imports and exports would both increase at a similar rate, this is explained by the economy's reliance on imports for consumption and investment.

The PMA's pessimistic scenario assumes a sharp deterioration in political and security conditions; a decrease in the number of Palestinian workers in Israel; a tightening of restrictions on the movement of people and goods; an increase in days of closure for workers and trade; a proliferation of barriers to import and export; Gol withholding tax revenues; a decline in foreign aid from donor countries to support the budget and development expenditure; and a delay in the transfer of funds dedicated to restructuring Gaza. Real GDP would fall by 3.9%, real GDP per capita would fall by 6.7% and unemployment would rise to 31%. Consumption and investment would decline by 5.3% and 14.3% respectively, and reduction in economic activity would lead to a narrowing in the trade deficit of 14.2%, with total import reduction outstripping the decline in exports.

Recent developments, with Israel withholding tax revenues (see below) and concerns over the US Congress withholding aid flows to Palestine, are closer to the pessimistic scenario and are not encouraging signs for 2015.<sup>4</sup>

## Clearance Revenues

As the Bulletin went to print, the Gol had not transferred tax revenues worth around \$125m to the PNA. The decision followed recent political moves by the PNA, including its decision to join the Rome Statute of the International Criminal Court in The Hague.<sup>5</sup>

Under the terms of the 1994 Paris Protocol guiding the economic relations between Israel and Palestine, Israel collects VAT, customs and income tax from Palestinians

working in Israel and Israeli settlements on behalf of the PNA, and transfers it on a monthly basis. The so-called clearance revenues are crucial to the Palestinian budget, constituting around two thirds of total domestic revenues, or more than three quarters of the PNA's wage bill.<sup>6</sup> As a result of the recent decision by the Gol, around 180,000 public employees, including members of the security forces and public service pensioners, faced substantial delays to their December salary payment.

The withholding of clearance revenues poses serious risks to the PNA's already delicate fiscal situation. Towards the end of 2012, a similar measure by the Gol seriously hindered the PNA's ability to provide basic services and triggered public sector strikes and protests.<sup>7</sup> If sustained, the non-payment of public sector wages, allied to the potential inability to provide social transfers to 90,000 households, could negatively affect consumption and therefore overall economic growth. At the same time, it could result in increased risks for local banks, heavily exposed to the PNA and its employees, in the event of a rise in the number of non-performing loans. Private sector suppliers, already suffering from lengthy delays in PNA payments, are also likely to suffer.

PNA officials approached Arab donors to secure extraordinary financial support to mitigate shocks in the public accounts. As the Bulletin went to press, it was announced that civil servants would likely receive 60% of their December salaries by the end of the week as a result of loans from local banks and Arab donations.<sup>8</sup>

## Gaza Reconstruction Mechanism

In September 2014 a trilateral agreement was reached between the PNA, the Gol and the United Nations (UN) on the Gaza Reconstruction Mechanism (GRM).<sup>9</sup> The GRM aims to ensure that construction materials are used exclusively for their intended purpose, with the UN monitoring compliance. In recent weeks, the General Authority of Civil Affairs has begun releasing regular data on levels of activity under this mechanism.

As of 4 January 2014, over 42,000 individuals had submitted damage assessments. 38,710 individuals requesting construction materials to reconstruct their homes had received approval under the GRM to purchase the necessary materials and almost all had been notified.<sup>10</sup> A total of 35,294 metric tonnes (MT) of construction materials had so far been imported to the Gaza Strip by 13 private sector vendors, of which 30,918 MT had already been accessed by 15,602 individuals.

4 [politi.co/1Akq8ER](http://politi.co/1Akq8ER)  
5 [reut.rs/144RFkF](http://reut.rs/144RFkF)

6 [bit.ly/1y2NPo4](http://bit.ly/1y2NPo4)  
7 [www.portlandtrust.org/publications/peb/issue-76-january-2013](http://www.portlandtrust.org/publications/peb/issue-76-january-2013)  
8 <http://english.wafa.ps/index.php?action=detail&id=27623>  
9 [bit.ly/11Nz4Hn](http://bit.ly/11Nz4Hn)  
10 [bit.ly/1u6qug1](http://bit.ly/1u6qug1)

Shelter repair assessments continue to be provided to the Ministry of Civil Affairs for processing, with over 100,000 individuals ultimately expected to access construction materials for shelter repairs/rehabilitation. However, the GRM has received criticism from the private sector and individuals for the slow pace of delivery to date. Further, the PNA has noted that the mechanism is merely a tool to enable reconstruction and has called on donors to fulfil their pledges of support for Gaza's reconstruction given at the October Cairo Conference.

## West Bank Oil Exploration

Dr Mohammad Mustafa, Deputy Prime Minister and Minister of National Economy of the PNA, announced the relaunch of an international tender for oil exploration in the West Bank on 24 December 2014.<sup>11</sup> The bidding process will close on 31 March 2015. This follows an initial tender last year which, according to the PNA, was undermined by political volatility leading only one bidder to apply.

The Rantis-1 block, which extends over 432 km<sup>2</sup> from north of the city of Qalqilya to the west of Ramallah, is situated adjacent to areas licensed by Israel for petroleum exploration and introduction to Israeli company Givot Olam Oil Ltd.<sup>12</sup> The field is estimated to hold 30-186 million barrels of oil and will potentially generate \$1bn in revenues for the PNA. The Palestine Investment Fund will participate in the project through a joint venture with the winning bidder, maintaining at least a 25% ownership stake. According to Dr Mustafa, "the existence of oil in Palestine is a highly promising opportunity for the Palestinian economy", and "having local oil supply will alleviate some of the costs borne by the Palestinian economy on oil imports". However, one note of caution is that parts of Rantis-1 are located in areas classified as Area C according to the Oslo Accords, which may complicate exploration and future development.

## Inflation During 2014

The Palestinian Consumer Price Index (CPI) increased by 1.73% during 2014 compared to 2013, rising by 3.84% in East Jerusalem<sup>13</sup>, 2.85% in Gaza and 1.2% in the West Bank.<sup>14</sup> This mirrored almost exactly the 1.72% rise experienced in 2013, although the geographical drivers varied (1.81% in East Jerusalem, -0.76% in Gaza and 3.10% in the West Bank).<sup>15</sup> Alcoholic beverages and tobacco experienced the largest price rises at 11.8%, followed by medical care at 8.71%. The most significant price reductions were for transportation costs (-2.86%) and communications (-2.57%). This trend of low inflation

11 <http://bit.ly/1xu2DHs>

12 <http://www.palexploration.ps/pdf/Rantis-1-RFP-17-Dec-2014.pdf>

13 Defined as those parts of Jerusalem annexed by Israel in 1967

14 [bit.ly/11NxDSp](http://bit.ly/11NxDSp)

15 [bit.ly/1BvGBKA](http://bit.ly/1BvGBKA)

can in part be attributed to the poor growth performance across the economy.

## Balance of Payments

In Q3 2014 the current account deficit amounted to \$246.3m, a level significantly lower than in any quarter in recent years.<sup>16</sup> This represents a 55.3% fall from the level observed in the previous quarter, and a similar decline (57.8%) with respect to Q3 2013. The deficit constituted 8.1% of quarterly GDP at current prices, down from 16.6% in Q2 2014. The current account deficit has traditionally been mainly caused by the consistently high deficit in the trade balance of goods (\$1.36bn in Q3 2014, or 44.9% of quarterly GDP), which decreased by 6.8% compared to the previous quarter and increased by 11.8% from Q3 2013. However, this quarter saw an unusually large surplus of current transfers at \$803.5m, representing an increase of 34.3% compared to the previous quarter and 123.5% from Q3 2013. Data shows this is primarily driven by rising donor inflows to central government, which almost doubled to \$386.8m.

At the same time, the capital and financial account surplus experienced a fall from both the previous quarter (19.7%) and from Q3 2013 (25.7%). This decline can largely be attributed to substantial reductions in the net financial account.

**Table 2: Balance of Payments Q3 2013, Q2 and Q3 2014**

Item	Q3 2013 (USD millions)	Q2 2014 (USD millions)	Q3 2014 (USD millions)	Change (%) (Q3 2013- Q3 2014)	Change (%) (Q2- Q3 2014)
<b>Current Account</b>	<b>-\$583.5</b>	<b>-\$551.4</b>	<b>-\$246.3</b>	<b>-57.8</b>	<b>-55.3</b>
Trade Balance of Goods	-\$1,219.4	-\$1,462.7	-\$1,362.9	11.8	-6.8
Trade Balance of Services	-\$28.7	-\$41.6	-\$36.0	25.4	-13.5
Income Balance	\$305.1	\$354.7	\$349.1	14.4	-1.6
Balance of Current Transfers	\$359.5	\$598.2	\$803.5	123.5	34.3
<b>Capital and Financial Account</b>	<b>\$501.2</b>	<b>\$463.6</b>	<b>\$372.2</b>	<b>-25.7</b>	<b>-19.7</b>
Net Capital Account	\$100.3	\$76.0	\$78.5	-21.7	3.3
Net Financial Account	\$400.9	\$387.6	\$293.7	-26.7	-24.2

Source: PCBS and PMA

## International Investment Position

In line with a medium-term trend, in Q3 2014 the stock of investments of Palestinian residents outside Palestine (total external assets) exceeded investments in Palestine by non-residents (total foreign liabilities). Palestine's international investment position (defined as external assets minus foreign liabilities) stood at \$1,171m, marking a 19.5% increase compared to the previous quarter.<sup>17</sup> The observed change can largely be attributed to capital flight from Palestine by both foreign and local investors during Q3, likely due to the Israeli military operation in Gaza and wider political uncertainty. Palestinian direct and portfolio investments abroad both increased (by 6.1% and 4.4% respectively), while portfolio and other investments

16 [www.pcbs.gov.ps/portals/\\_pcbs/PressRelease/Press\\_En\\_BoPQ32014E.pdf](http://www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_BoPQ32014E.pdf)

17 [pcbs.gov.ps/portals/\\_pcbs/PressRelease/Press\\_En\\_IPEDStatQ32014E.pdf](http://pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_IPEDStatQ32014E.pdf)

in Palestine by non-residents also fell (by 6.3% and 7.3% respectively). The largest swing was a \$122m decline in currency and deposits held by foreign investors in Palestine.

## Stock Exchange Performance in 2014

In December the Al-Quds index increased by 6.1% from the previous month, reaching a peak of 511.77 points on the last day of trading.<sup>18</sup> A total of 12.5m shares worth \$22.6m were traded in December. This marked a decrease of 8.9% in the volume and 16.2% in the value of traded shares from November. Market capitalisation increased over the month by 4.4%, reaching \$3.19bn.

The year 2014 saw the Al-Quds index follow a downward trend (Figure 1). Overall, Al-Quds dropped by 5.5% between the opening (541.45 points) and close (511.77 points) of trading for 2014. The index rose by over 10% in January, reaching its highest point for 2014 of 603.03 points on 2 February. However, this was followed by a period of gradual decline in February and March, with the index falling back to its starting levels for the year by early April. This downward trend continued in Q2, and by the end of June the index had fallen 16.6% from the February peak to 502.81 points. Perhaps surprisingly, the index actually increased during the Gaza war and closed at 523.32 points on 27 August, with the PEX announcing strong aggregate net profits of listed companies had grown 13.6% in the first half of 2014. The coming months brought a period of sustained decline in performance, and the index reached a yearly low of 482.45 points on 30 November. December brought some improvement, but overall the story for the year is one of declining performance and relatively high volatility. Most sectors followed a similar trend to the overall index, but the insurance and industry sectors did not track the index so closely and exhibited higher volatility. Only the insurance index experienced positive performance over the year, rising by 2.8%. The services sector performed the worst, falling by 5.8%.

**Figure 1: Al-Quds Index, 2014**



Source: PEX

Throughout 2014, a total of 181.5m shares were traded on PEX with an overall value of \$353.9m. The most traded sector by value was services, (33.7%), followed by banking and financial services (31.5%) and investment (30.9%). With respect to market capitalisation, services accounted for 44.6% of the total, banking and financial services for 26.4%, investment for 17.1%, industry for 8.6% and insurance for 3.3%.

The top five performers in 2014 were Nablus Surgical Center (whose share price increased by 58.2%) Palestinian for Distribution & Logistics Services (+29.4%), Global United Insurance (+28.8%), Al-Takaful Palestinian Insurance (+25.9%) and The Vegetable Oil Industries (+20.9%). The companies with the largest decreases in stock price were Global Telecommunications (-55.6%), Palestine Plastic Industries (-42.4%), Palestine Electric (-27.5%), The Arab Real Estate Establishment (-23.7%) and Palestine Islamic Bank (-21.4%). The most traded stocks in terms of value were Palestine Telecommunications (\$101.0m or 28.6% of the total), Palestine Development & Investment (PADICO) (\$88.7m or 25.1%) and Bank of Palestine (BOP) (\$59.2m or 16.7%). With respect to volume, the companies with the highest liquidity traded on PEX were PADICO (54.1m or 29.8% of the total), BOP (20.6m or 11.3%) and The National Bank (16.7m or 9.2%).

<sup>18</sup> [www.pex.ps/PSEWebSite/publications/PEXIssue-06Jan2015.pdf](http://www.pex.ps/PSEWebSite/publications/PEXIssue-06Jan2015.pdf)

## The Portland Trust



The Palestinian Economic Bulletin is prepared by the Palestine Economic Policy Research Institute (MAS) and edited by The Portland Trust. Please send any comments, suggestions, or complaints to [feedback@portlandtrust.org](mailto:feedback@portlandtrust.org)

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