

***CHALLENGES TO REFORMS AND
ECONOMIC FREEDOM IN THE
PALESTINIAN TERRITORIES***

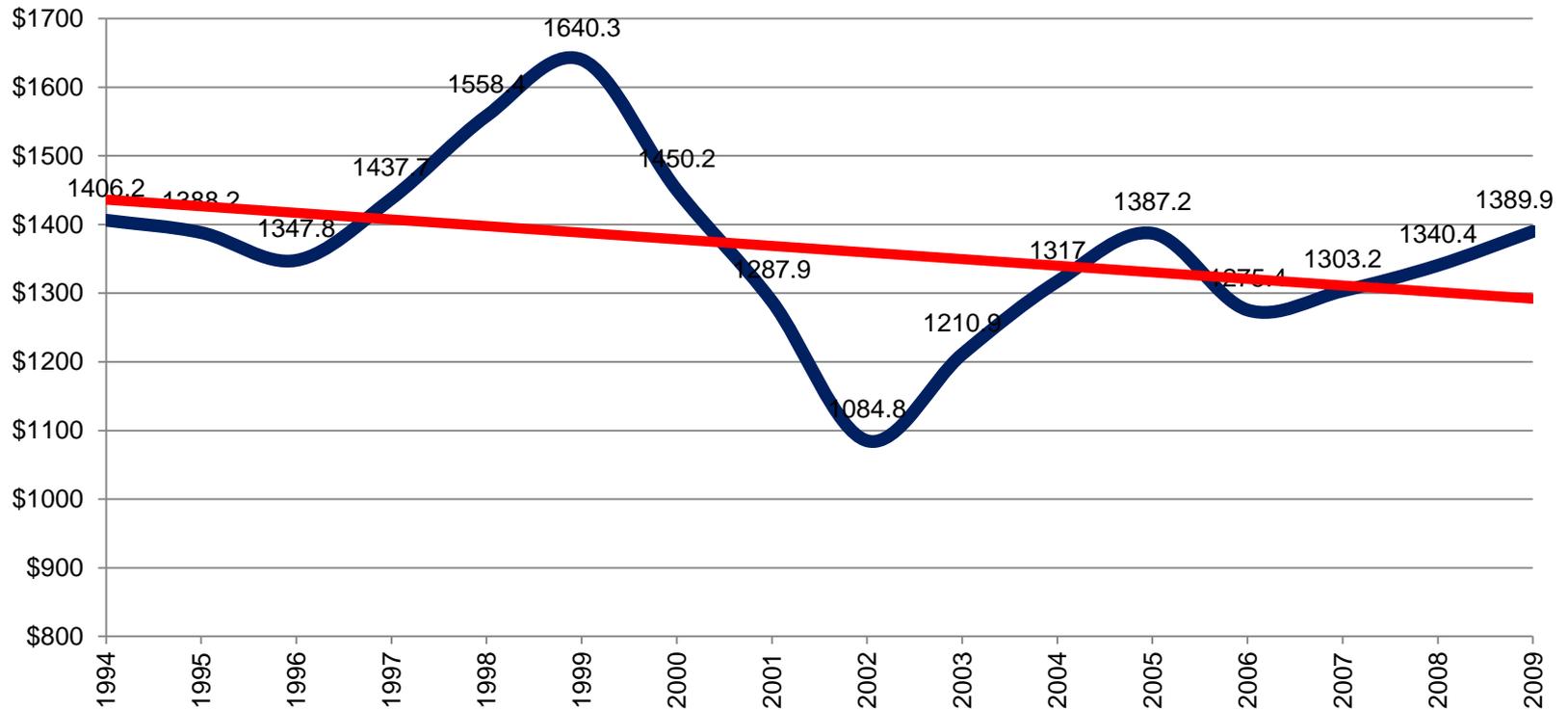
Dr. Mohamed Nasr

Background

- GDP growth in 2009 reached about 6.8 percent, and 5.9 percent in 2008
- GDP growth in 2010 is expected to reach 8 percent in the West Bank, and 16 percent in Gaza
- Could be misleading:
 - Not a trend
 - Unsustainable
 - No improvement in economic freedom

Declining Living Standards

GDP per capita



Unsustainable

- PNA's economic growth is driven largely by public spending, which in turn is financed by international donors.
- External Assistance: US\$1.4 billion in 2009, US\$1.8 billion in 2008, US\$1 billion in 2007
- This growth is unsustainable.
- Without removing restrictions on movement and access, sustainable growth cannot be sustained.

Poor Economic Freedom

- No ranking of economic freedom for Palestine
- Signs of weak and deteriorating economic freedom in WBG
- Examples follow

Size of Government

- Government expenditure reached around 52% of GDP
- PNA employment increased to more than 25% of the labor force
- Spending on social protection increased significantly
- subsidization of utilities services remains high.

Reforms

- Reduce government spending
- Control growth of public employment
- Eliminate subsidization of utilities services (electricity, etc.)
- Stimulate private sector investment

Challenges

- Tight Israeli restrictions discourage private investment and employment, and force PNA to spend more
- Shrinking private sector and loss of employment opportunities in Israel force PNA to become increasingly important as a provider of jobs
- increased economic hardship force government to
 - subsidize delivery of utilities services
 - increase spending on social protection

Legal Structure and Security of Property Rights

- Different sets of laws applied to West Bank & Gaza.
- key laws and regulations are old and outdated, including IPR, and needs to be finalized and implemented.
- Court system suffers shortage of judges, prosecutors, and other staff.

Reforms

- Drafting new proposed laws, including modern IPR law, Company Law, Competition Law
- Implementing security sector reform
- Enforcing the rule of law
- Providing justice sector and security services with infrastructure, equipment and skills
- New judges and public prosecutors are being recruited
- New Anti-Corruption Commission has been established

Challenges

- Under Paris Protocol and Oslo agreements, PNA has Limited territorial, personal, and functional jurisdiction.
- The Palestinian Legislative Council (PLC) is paralyzed since 2007 due to:
 - Internal conflict
 - Israel's arrest of PLC members.
- New laws must be adopted as presidential decrees, which often delays reform efforts.

Access to Sound Money

- PMA was established in 1995 as part of the Paris Protocol, which regulates monetary issues in PT.
- PMA cannot issue currency. It is mainly concerned with regulating banking operations, supervising and restructuring domestic banking sector.
- PMA plans to become a full-fledged central bank
- PMA introduced and implemented many institutional and legal reforms, including new automated payments system, credit bureau, and strong anti-money laundering law.

Challenges

- Paris Protocol imposed severe limitations on monetary policy instruments available to the PNA and created substantial space for unilateral Israeli action.
- Use of three currencies in PT imposes excessive risk.
- Israeli banks have been refusing to accept deposits from Palestinian banks
- Israel frequently prevents PNA from transferring cash to the Gaza Strip

Freedom to Trade Internationally

- Paris Protocol governs trade relations between the PNA, Israel and ROW.
- Most customs procedures and tariff measures are based on Israeli norms, and to a large extent, Israeli control.
- Imports of many products under the PNA's authority are still subject to quantitative restrictions or Israeli standards.
- PNA has no functioning airport or seaport.
- It has no control over its borders, territorial waters or airspace.

Reforms

- PA has taken many steps to facilitate and increase foreign trade and encourage FDI such as:
 - signing free trade agreements with many countries.
 - obtaining observer status in the WTO
 - providing incentives to foreign investors under free admission principle (Law on Encouragement of Investments)

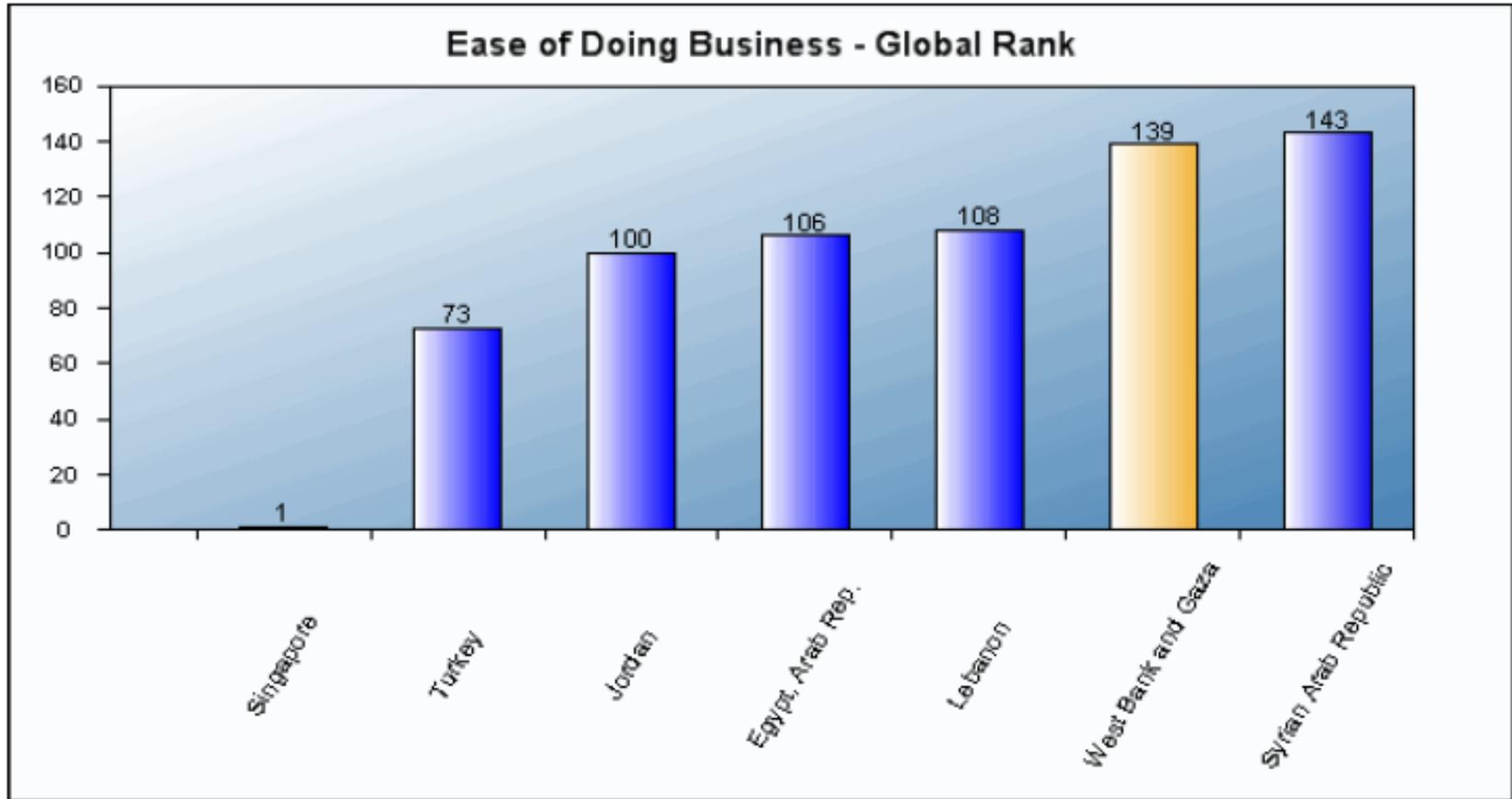
Challenges

- Constraints imposed by Paris Protocol restricts Palestinian economic relations with other countries
- Israeli control over borders , restriction on movement and access in the WB and isolation of Gaza, closures and political instability prohibit free trade, discourage domestic and foreign investment, and compromise Palestinian's ability to benefit from free trade agreements
- High dependency on Israeli market limits trade with other countries and renders Palestinian economy highly susceptible to shocks resulting from closures and political instability.

Regulation of Credit, Labor, and Business

- Doing Business 2010 Report: published by the World Bank have shown weak performance
- Out of 183 economies, the overall "Ease of Doing Business" ranking of the WBG is 139 in 2010, compared with 137 a year earlier.

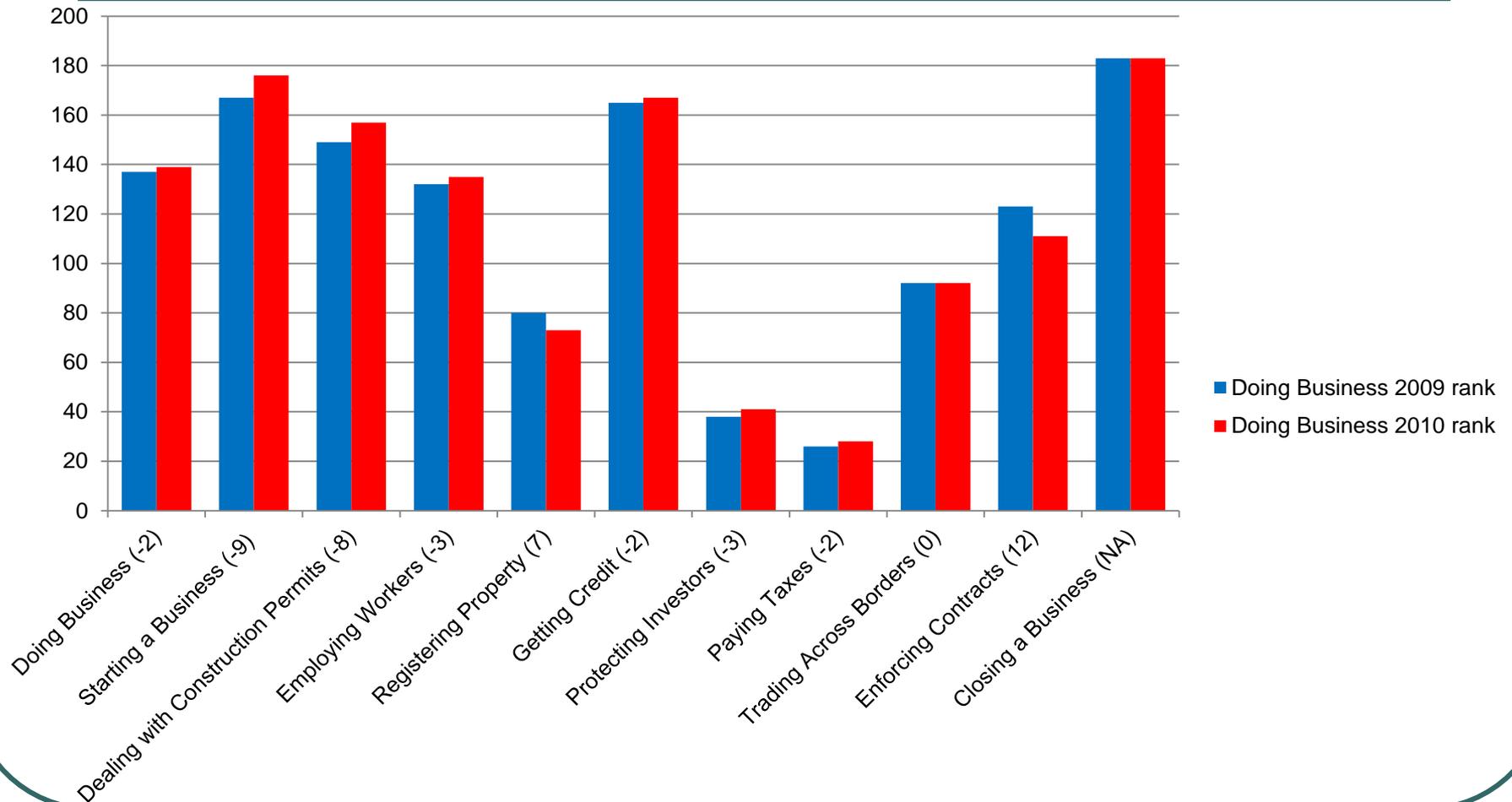
Overall Ranking



Other Indicators

- The situation is worse for starting a business indicators, where WBG is ranked 176.
- There has been deterioration in all variable in 2010 (except for registering property and enforcing contracts).

Ease of Doing Business



Reforms

- The World Bank acknowledged some reforms in certain areas, such as
 - Speeding up contract enforcement.
 - Courts now have enforcement judges
 - computerized case management software.
 - Property registration was expedited.
- Many of these reforms are included in the PRDP

Conclusions

- However, the most serious challenge to these reforms and, hence, to economic freedom and growth remains the Israeli occupation and policies
- The borders, airspace, water rights and communications are still under Israeli control; so is 60% of the West Bank;
- Gaza is isolated and exports from there are prohibited;
- Access to the majority of the West Bank's land, water and natural resources is severely curtailed;
- East Jerusalem is beyond reach;

These are the real challenges

- The ability of investors to enter into Israel and the West Bank and Gaza is unpredictable;
- Israeli policies to discourage visiting diaspora and foreign investors.
- Israel's freeze on clearance revenues;
- Expansion of Israeli settlement
- Construction of the Separation Wall,
- The closures, incursions and checkpoints,
- The continued lack of political progress,

The conclusion of the World Bank

Without removing these obstacles, economic growth will not be sustainable, the PNA will remain donor dependent, and its institutions - no matter how robust - will be unable to underpin a viable state.

Size of Government: Expenditures, Taxes, and Enterprise

