MAS

Palestine Economic Policy Research Institute

Round Table (1)

Internal Division and the Private Sector: Burdens and Ways of Relief

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The political disunity crisis in the Occupied Palestinian Territory (OPT) since June 2007 has not only negatively affected the public sector, but torn the fabric of the private sector and impeded the growth of the Gaza Strip economy. Four years later, the Palestinian political process remains broken, in a chronic state of uncertainty. The existing division between Hamas and Fatah has forced policy-makers to operate in the short run and the business sector to disregard the long-term planning necessary for the economic development of the OPT.

Due to the gravity of this predicament and its dramatic repercussions on the Palestinian economy, the Palestine Economic Policy Research Institute (MAS) found it necessary to facilitate an open dialogue on the burdens of the internal division. On March 23rd, 2011, MAS hosted the first of a series of roundtable discussions with local experts and stakeholders. Representatives of the public and private sector, judicial and legislative authorities, civil-society organizations, and academia all attended the event.

Mr. Samir Hulileh, Chief Executive Officer of PADICO, opened the forum with a speech that effectively set the tone for the subsequent open discussion among attendees. This was followed by an open dialogue and a commentary on the situation in the Gaza Strip. Afterward, the attending stakeholders participated in an in-depth discussion on the obstacles faced by the private sector as a result of the political and geographical division between the West Bank and the Gaza Strip. The dialogue focused on evaluating the measures and procedures taken by the authorities in both the West Bank and Gaza to resolve the impeding strains of political disunion. The roundtable concluded with an open-space session, offering the participants the opportunity to propose their own ideas and practical recommendations to ease the burden of a divided Palestinian territory.

Internal and International Trade

The volume of internal trade between the West Bank and Gaza has decreased substantially in recent years due, in large part, to the political division in the OPT and the Israeli siege imposed on the Gaza Strip. As a result of the incessant restrains on internal trade, distinct consumption patterns emerged in Gaza as cheap Egyptian goods flooded the local market via smuggling tunnels. These consumption patterns impacted negatively internal trade between the West Bank and Gaza, and are expected to continue long after political reconciliation is attained. For example, in Gaza, the increased availability of Egyptian petroleum products caused discrepancies in the competitive advantage of industrial enterprises in favor of enterprises using low-cost fuel in Gaza since the West Bank imports all of its petroleum products from Israel. This will undoubtedly exacerbate the decline in trade between the West Bank and the Gaza Strip.

In large part due to the Israeli siege, since 2007 exports from Gaza fell from 5,747 trucks per year to only 20 trucks in 2009. The number of trucks entering Gaza decreased from 160,000 in 2005 to 60,000 in 2010.

Banking and Monetary Transactions

The internal division in the OPT affected banking institutions significantly. Since 2007, they have had to cope with the consequences of political volatility and the challenges that emerged from the frequently changing economic climate. For instance, the PNA Minister of Finance in the West Bank issued a resolution ordering the freezing of all PNA bank accounts in the Gaza Strip and the immediate transfer of all PNA deposits to banks located in the West Bank. Following this development, the authority in Gaza began performing financial transactions through the Postal Bank and the Islamic National Bank, both of which are affiliated with Hamas. These decisions resulted in a significant loss of deposits in the Gaza banks and a sharp decline in their banking activities. Banks performance along with their credit facilities also deteriorated as a result of the suspension of operations in the Palestinian land authority, which in turn affected the ability of borrowers to provide collaterals. Similarly, the PNA issued a resolution to exempt individuals and firms in the Gaza Strip from taxes and fees; however, the authority in Gaza has since enforced the payment of the latter. Such contradicting measures caused widespread confusion and disorder among banks and firms in the OPT.

Data show that bank performance and the availability of credit facilities have severely deteriorated since 2006. Credit facilities to Gaza decreased from US $524.4 million in 2006 to US $192.3 million in 2010. Not only has supply decreased significantly since the onset of internal division, but demand has also declined as a result of the deteriorating investment climate in Gaza. Moreover, banks operating in Gaza faced a plethora of legal difficulties as a direct consequence of Palestine's paralyzed judicial system. Additionally, all operations between Israeli and Gaza banks have been indefinitely ceased, which led to cash illiquidity in Gaza and money-transfer mechanism between the West Bank and Gaza.

Investment Climate

The investment climate in the OPT has grown increasingly volatile as a result of years of unmitigated internal division. This fact is most evident in the Gaza Strip, where the volume of investments as well as the number of registered firms and operating enterprises has dramatically decreased since 2007 as a result of the rising pressure and widespread uncertainty caused by contradicting decisions made by opposing authorities. Further illustrating the volatility of the investment climate in Gaza, many firms moved their headquarters to the West Bank to avoid the procedural complications that may arise in Gaza.

Public Finance

Collecting taxes in the OPT became increasingly troublesome as no coordination currently exists between the PNA and the Hamas-led authority in Gaza. The decision of PNA President Mahmoud Abbas to exempt individuals and firms in Gaza from fees and taxes alone reduced the annual budget of the PNA by about NIS 82 million, compared to 2005. Further complicating the public finance sector, Gaza importers no longer provide the PNA with the required unified clearing tax invoices for goods imported into the OPT from Israel. It is estimated that the collective burden caused by the internal Palestinian division has deprived the PNA's budget of NIS 150-200 million.

Firms with branches both in the West Bank and the Gaza Strip, and those which moved their headquarters from Gaza to the West Bank, face tax-filing complications at the Income Tax Departments, as no facilitations or exceptions are given to firms from the authorities in the West Bank and the Gaza Strip. Similarly, the authority in Gaza currently imposes income taxes on commercial cargo arriving in Gaza from the West Bank and not – as the law requires – on the net commercial transactions of enterprises at the end of each fiscal year. These procedures hamper the flow of trade between the West Bank and Gaza and create more obstacles in front of the private sector. Moreover, the continuity of the internal division obstructs international aid flow to Gaza and slows down the execution of the investment package approved by the international community at the Sharm Al-Sheikh Conference in 2009 to rebuild Gaza after Operation Cast Lead.

Recommendations

The following measures and mechanisms should be devoted to the process of mitigating the burdens of division:

Creating a private-sector standing committee with representatives from both the West Bank and the Gaza Strip to communicate and resolve complaints about the governmental procedures and practices in both parts of the country: mainly, double taxation, fees, licenses, etc.

Meetings between this private-sector standing committee and the authorities in the West Bank and the Gaza Strip with the main objective to formulate strategies to ease the burden of internal division on the business community. This major goal will be accomplished through the achievement of two specific objectives: first, preventing the institutionalization of the existing division; and second, avoiding the imposition of additional restrictive procedures on the business environment by the PNA or De-facto government in Gaza, which negatively impact the private sector development.

Rehabilitation and revitalization of Gaza Strip and its private sector: The PNA must enhance its diplomatic efforts to end the Israeli siege on the Gaza Strip immediately, including the implementation of the Access and Movement Agreement of November 2005. This agreement allows the free movement of individuals and goods between the Gaza Strip and the West Bank, and the reopening of Rafah border passage with Egypt, so that Gaza residents can have free access to the outside world. The development effort in the Gaza Strip should comprise a comprehensive reconstruction and rehabilitation process, including the revitalization of the private sector as one of the main components.