PALESTINE ECONOMIC POLICY RESEARCH INSTITUTE (MAS)

Palestine Economic Update

August 2024

Key Messages :

- The PA's 2024 Emergency Budget faces a significant ILS 5.5bn deficit due to sharp declines in domestic (21.4%) and clearance revenues (21.7%).
- The PMA warned that Israel's refusal to accept excess Israeli Shekel banknotes could jeopardise trade and the broader Palestinian economy.
- A new EU project aims to support the Palestinian private sector and boost exports. Trade with the EU remains minimal despite long-lasting trade agreements due to movement and access restrictions.
- Israel's expansion of cellular coverage in the West Bank, including a new tower near Ramallah, threatens Palestinian telecom operators, exacerbated by delays in deploying 4G

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1. PA Emergency Budget 2024

On 22 July, the Palestinian President approved an emergency budget for the 2024 fiscal year with a deficit of ILS 5.5bn, an 181.5% increase compared to 2023.[1] The Palestinian National Authority's (PA) deep fiscal crisis, the ongoing war on Gaza and the heightened uncertainty surrounding public finances drove the adoption of an emergency budget. The fiscal situation has worsened significantly since the war on Gaza began, with Israel escalating its deductions from PA clearance revenues. In the first half of 2024, Israel withheld ILS 1.8bn in clearance revenues, a 312.9% increase compared to the same period in 2023. Total Israeli deductions and withheld amounts accounted for 67.8% of the PA's clearance revenues in the first half of 2024, totalling ILS 3.0 bn.[2]

Table 1: PA budget for 2023 and 2024, million ILS (accrual basis)

Item	2023 (budget)	2023 (actual)	2024 (budget)
1. Net public revenues	**18,284.6**	**17,749.9**	**13,951.4**
A. Domestic revenues	6,607.6	5,988.2	4,704.6
B. Clearance revenues	12,003.0	11,917.7	9,336.0
C. Tax rebates (-)	326.0	156.0	89.2
2. Public expenditure and net lending	**18,868.7**	**18,341.8**	**17,898.0**
A. Salaries and wages	8,679.5	8,356.4	8,469.1
B. Social contributions (government)	854.2	818.8	829.9
C. Social transfers	3,539.1	3,028.5	3,230.8
D. Operating expenses	2,718.9	3,154.6	2,506.1
E. Net lending	1,261.0	1,342.4	1,250.0
F. Other expenditures	1,816.0	1,641.1	1,612.1
3. Current account deficit before financing	**-584.1**	**-591.9**	**-3,946.6**
Development expenditure	2,139.1	1,347.4	1,512.1
4. Total deficit before aid and grants	**-2,723.2**	**-1,939.3**	**-5,458.7**
A. Direct budget support	824.0	755.2	1,965.0
B. Development expenditure support	680.0	560.2	544.5

Source: Palestinian Ministry of Finance

1.1 Public revenues and spending

The budget anticipates a 21.4% drop in revenues for 2024, falling to ILS 14.0bn. This is driven by a 21.4% decrease in domestic tax revenues (to ILS 4.7bn) and a 21.7% decrease in clearance revenues (to ILS 9.3bn, before accounting for withheld amounts). The decline is attributed to the sharp downturn in economic activity and trade following the war on Gaza. In Q1 2024, Palestinian GDP fell by 10.2% compared to Q4 2023, and 34.9% below the corresponding quarter in 2023.[3] Total Palestinian imports were down 28.4% in the first half of 2024 compared to the same period in 2023, while total exports declined by 13.8%.

Government spending is targeted to reach ILS 17.9bn in 2024, a 2.4% decrease from last year. The Ministry of Finance announced that the emergency budget includes austerity measures such as cutting operating and capital expenses and keeping development expenditures at a minimum.[4] It focuses on

1 Percentage changes throughout this text are compared with the actual figures of 2023 based on the information published by the Palestinian Ministry of Finance: https://www.pmof.ps/internal.php?var=11&tab=01

2 See the June 2024 issue of the Palestine Economic Update for more information about deducted and withheld clearance revenues: https://mas.ps/publications/10412.html

3 https://www.pcbs.gov.ps/site/lang__en/741/default.aspx

4 https://www.wafa.ps/Pages/Details/100005

reducing financial ceilings for government institutions without compromising service quality and will be implemented based on the availability of daily cash liquidity.

The Ministry also confirmed its ongoing development policy, which includes structural reforms of the revenue system, gradually reducing medical transfers, and prioritising critical sectors like health, education, social protection, and security. Additionally, the ministry plans to curb net lending costs (to cover unpaid utilities bills of Palestinian consumers) through stricter collection policies and linking municipal support to efforts in lowering net lending.

The 2024 budget allocates an additional ILS 100mn to support the Gaza Strip, supplementing the approximately five billion shekels the government spends on the region annually. These amounts will be inadequate in the face of the need to provide basic needs to 2.5 million impoverished, displaced people in Gaza Strip.

1.2 Budget Support

Faced with unprecedented declines in public revenues, the PA anticipates renewed foreign aid to help alleviate the projected deficit. The 2024 budget assumes a 160.2% increase in direct budget support to ILS 2.0bn. However, support for development expenditures is expected to decrease by 2.8% to ILS 511.5m. This leaves the PA with a current account deficit after budget support of ILS 2.0bn and a total budget deficit after support of ILS 3.0bn. Considering the withheld clearance revenues and assuming the same level of deductions in the second half of 2024 as in the first, the budget cash deficit before financing is projected to reach ILS 5.6bn.

On 19 July, the EU announced €400m in emergency funding for the PA, including €150m earmarked for public salaries and pensions, of which €43m were disbursed on 9 August.[5] The emergency package includes loans and grants, with disbursement contingent on agreed-upon PA reforms. This aid is part of the EU's broader strategy, the Comprehensive Programme for Palestinian Recovery and Resilience, which envisions a reform-driven stabilisation of PA finances by 2026 and includes a donor coordination platform. This latest package reinforces the EU's position as the leading international donor to the Palestinian people.[6]

1.3 Public debt and arrears

To manage its fiscal shortfall, with limited access to international capital markets and bank financing constraints for prudential reasons, the PA continued to accrue a large and growing stock of arrears to the private sector, the pension fund, and public employees. The PA net accumulated arrears reached ILS 15.7bn in June 2024, a 39.8% increase compared to June 2023. Private sector arrears account for 29.4% of this sum, around ILS 4.6bn, the bulk of which is owed to hospitals, pharmaceutical companies, and contractors. The remaining amount, around ILS 11.1bn, is arrears to the civil service pension fund, and to public employees due to partial salary payments since 2019. The large and growing stock of arrears drains liquidity from the local economy and risks further economic instability.

The PA's public debt stood at ILS 14.9bn (around $4 bn) in June 2024, a 10.3% increase compared to June 2023. This represents 22.6% of the 2023 Palestinian GDP, still below the limit permitted by the Law on Public Debt No. 24 for 2005 (40% of GDP). However, after accounting for arrears not included in the MoF public debt calculations, the PA's total public debt increases to ILS 30.6bn or 47.3% of GDP.

5 https://tinyurl.com/25tn86yf
6 https://tinyurl.com/yxbcttd4

2. Excess Shekel and PMA Initiatives

On 21 August, the Palestine Monetary Authority (PMA) issued a stern warning about the serious and imminent repercussions if the Bank of Israel (BoI) continues to refuse the acceptance of excess Israeli Shekel (ILS) banknotes accumulated in Palestinian banks.[7] The ongoing refusal prevents Palestinian banks from crediting their accounts at Israeli correspondent banks. The PMA warned that banks may soon be unable to finance trade operations or pay for goods and services from Israeli companies and suppliers.

2.1 Causes and Economic Implications

The recurring excess Shekel crisis, which can be traced back to 2009, has escalated recently, particularly in May when the Israeli Minister of Finance threatened not to extend a waiver that allows cooperation between Israel's banking system and Palestinian banks in the West Bank.[8] This recurrent issue stems from the BoI policy of capping and refusing to significantly increase the amount of ILS banknotes that Palestinian banks can transfer back to Israel, despite efforts by the Palestine Monetary Authority (PMA) to communicate the need for adjustments.[9] The original ceilings were set by the Paris Economic Protocol of 1994 when the Palestinian economy was small and had no banking system. The current ceiling is set at ILS 18bn per year, with some exceptional and occasional cash transfers allowed above the limits.[10] In 2022, Palestinian banks transferred ILS 25.5bn in banknotes to Israeli banks, compared to ILS 21.1bn in 2021.[11]

Historically, the primary source of excess ILS is the cash payment of the wages of Palestinians working in Israel. Palestine Central Bureau of Statistics (PCBS) records show that Palestinians working in Israel brought ILS 11.4bn into the Palestinian market in 2023, compared to ILS 14.7bn in 2022.[12] The numbers are likely higher, however, as there were large numbers of unrecorded Palestinians working in Israel and Israeli settlements, legally and illegally. Other factors include cash purchases by Palestinians from Israel in West Bank markets, excessive reliance on cash in daily transactions in Palestine, deep financial integration between the Palestinian and Israeli economies, growing financial inclusion, and a preference for the US Dollar (USD) and Jordanian Dinar (JOD) amongst Palestinian as a hedge against currency fluctuations.[13]

Excess ILS in Palestinian banks poses significant challenges, including high costs for storing, insuring, moving, securing, and administrating large amounts of cash, in excess of the amounts required to be retained by banks within PMA prudential guidelines.[14] By the end of June 2023, ILS deposits accounted for 44.6% of the total customer deposits in the Palestinian banking system.[15] In 2023, about 84% of the banking system's cash liquidity was in ILS, occupying large spaces in bank vaults.[16] Moreover, while this excess ILS cash continues to pile up in their vaults, banks are forced to borrow Shekels from the PMA as emergency liquidity assistance when they run low in their ILS correspondent account or swap JOD or USD for ILS to settle commercial transactions between their clients and Israeli merchants.[17] USD and JOD used as (borrowing or swap)

7 https://tinyurl.com/3m784nxb
8 https://tinyurl.com/mr6vtbuh
9 According to Article IV, paragraph 17 of the Paris Protocol on Economic Relations, the PMA has the right to convert excess NIS to foreign currencies at the BOI, up to the amounts determined per period and under specific arrangements.
10 https://tinyurl.com/uukp8x2c
11 https://tinyurl.com/mr3t685h
12 https://www.pcbs.gov.ps/statisticsIndicatorsTables.
13 https://www.aliqtisadi.ps/article/83449/
14 https://www.imf.org/en/Publications/CR/Issues/2022/09/15/West-Bank-and-Gaza-Selected-Issues-523402 - The PMA defines ILS cash surplus as any amount exceeding 6% of short-term deposits.
15 https://www.pma.ps/ar/Statistics//MonthlyStatisticalBulletin
16 https://tinyurl.com/mr3t685h
17 https://www.imf.org/en/Publications/CR/Issues/2022/09/15/

collateral cannot be lent out to customers, restraining lending for investment purposes. According to an IMF report in 2022, the costs associated with holding excess ILS lowers bank profits by about 20%.

Recent threats to end correspondence banking with Israeli banks and BoI's refusal to accept ILS banknotes could lead to stopping all financial transactions with Israel and stopping clearance of Palestinian banks' clients' cheques for the benefit of Israeli companies and service providers.[18] Palestinian banks' inability to process financial transactions can expose them to reputation risk among international correspondence banks, impacting banking stability.

The issue of excess ILS has long pressured banks in Palestine to impose stricter limits on ILS cash deposits, even after performing all due diligence in line with international banking rules. This reduces banks' ability to inject liquidity into the local market, disrupts the business cycle, and impact the broader economy.[19] This also increases businesses' reliance on non-banking instruments and, thus, their risk exposure, further straining the Palestinian economy. In response to the excess ILS issue, the PMA has long been negotiating with the BoI to raise the ceiling of ILS transfers and is working to decrease cash reliance by promoting electronic payment systems.

2.2 IBURAQ

On 23 July, the PMA officially launched the Instant Payment System (IBURAQ) for interbank and digital wallet transactions.[20] This system enables real-time transaction clearing, with funds credited to the beneficiary's account instantly and the payer notified within 10 seconds. IBURAQ was first deployed in Gaza on May 8, allowing residents to conduct electronic transactions—particularly salary transfers for public and private sector workers—amidst severe cash shortages and the widespread destruction of banking, power, and communication infrastructure.[21] This highlighted IBURAQ's potential to drive the adoption of digital payment solutions across Palestine, particularly in sectors like retail, public transportation, and government fees. The system seamlessly integrates with the bill and service payment platform, E-SADAD, launched in late 2023. IBURAQ and E-SADAD are critical components of the PMA's digital transformation strategy. In 2022, 15.1% of the Palestinian adult population used at least one digital financial service.[22] Adopting digital payment systems, combined with the PMA's awareness campaigns and efforts to promote digital financial services, is expected to boost this percentage.

2.3 BADER

On 15 July, the PMA, in collaboration with the Ministry of Labour and the UK-funded TASDEER program, launched "BADER," an interest-free, commission-free loan program for Palestinian workers laid off by Israeli employers following the war on Gaza.[23] The program targets workers with valid permits issued before October 2023 and aims to provide affordable funding to help them start micro-enterprises and sustain their livelihoods amid the current economic crisis. The fund will disburse NIS 70mn in loans across multiple phases, with the first phase allocating NIS 30mn. Individual loans can reach up to NIS 60,000, with a repayment period of 4 years and a 6-month grace period. The PMA expects to support establishing over 500 projects through these loans. Applications can be submitted via the "Monshati" app or website, the PMA's flagship information centre for MSMEs.[24]

18 https://tinyurl.com/uukp8x2c
19 https://tinyurl.com/72xnpcnk
20 https://tinyurl.com/ycykdb6d
21 https://tinyurl.com/yc3uxcb8
22 https://www.financialinclusion.ps/item-1678961908
23 https://tinyurl.com/mtrj427k
24 https://monshati.ps/page/Worker-financing-program/ar

3. Israel Cellular Takeover in the West Bank

On 15 July, the Israeli Minister of Communications announced the inauguration of a new cellular tower in the Beit El settlement near Ramallah, within a broader effort to expand Israeli cellular coverage in the West Bank.[25] This initiative is part of an ILS 50mn project funded by the Israeli Ministry of Finance, aimed at expanding Israeli cellular coverage by adding dozens of new towers. These towers will augment the network of over 560 Israeli towers across the West Bank, primarily in Area C.[26] The expansion follows a 2021 decision by former Israeli Minister of Communications Benny Gantz to boost 4G coverage for Israelis from 75% to 95% of the West Bank.[27]

These new developments threaten the viability of Palestinian mobile and internet providers, who are suffering from the destruction of all major communication networks in Gaza and declining economic activity in the West Bank.[28] Palestinian telecommunication value added declined by 20.2% in Q1 2024 compared to the corresponding quarter in 2023, with a 17.7% drop in the West Bank and a 92.7% decline in the Gaza Strip.[29]

3.1 Restrictions on Palestinian internet infrastructure

Israel granted approval for 4G broadband in the West Bank in late 2022, following over a decade of restrictions on 3G and prolonged delays in approving newer cellular technologies.[30] Although 4G deployment was initially expected to take at least 12 months, progress has remained stagnant, and there is no clear timeline for activation.[31]

Israeli restrictions have long impeded the development of the Palestinian mobile sector by limiting access to critical infrastructure, including submarine cables, microwave systems, and optical fibres.[32] Despite 4G being available in Israel since 2014 and 5G since 2020, 3G only became available in the West Bank in 2018 due to Israeli restrictions, while those in Gaza are still confined to 2G frequencies.[33] These restrictions have put Palestinian telecom operators at a significant competitive disadvantage, leading to higher deployment costs, increased prices for consumers, and lower wages for employees. Meanwhile, Israeli operators, who have access to over 60% of the West Bank's territory and infrastructure, have captured around 20% of the West Bank's mobile broadband market, particularly among Palestinians who work in Israel or its settlements.[34] Between 600,000 and 800,000 Israeli SIM cards are activated in Palestinian territories, a figure that has been rapidly increasing each year.[35] A 2016 World Bank report estimated that Palestinian cellular companies lost between $436mn and $1.5bn in potential revenue over three years due to Israeli-imposed frequency and infrastructure restrictions, mainly related to delays in the roll-out of 3G.[36]

4. EU-PALTRADE Export Promotion

On 18 July, PALTRADE and the EU signed a three-year, €3mn project to support the Palestinian private sector.[37]

25 https://www.gov.il/en/pages/15072024
26 https://tinyurl.com/ycyr9d53
27 Ibid
28 https://wafa.ps/Pages/Details/100143
https://theintercept.com/2024/06/21/israel-gaza-internet
29 https://www.pcbs.gov.ps/statisticsIndicatorsTables.
30 https://www.timesofisrael.com/israel-pledges-to-finally-permit
31 https://tinyurl.com/tjbne3at
32 https://tinyurl.com/3yk3h8sv
33 https://www.jpost.com/jpost-tech/5g-network-officially
34 https://tinyurl.com/yc37s6jf
35 https://www.bnews.ps/ar/node/23633
https://tinyurl.com/mrxv2exc
36 https://tinyurl.com/ycyzu4kj
37 https://paltrade.org/single-news/38/en

This fund will finance a comprehensive program designed to strengthen economic infrastructure and bolster MSMEs in Palestine. The project aims to stimulate economic growth, enhance private sector capacities, and create job opportunities. A key focus is improving trade between Palestine and the EU by developing the PALTRADE Commercial Information Unit, establishing a storage and distribution centre for Palestinian products targeting European markets, and implementing various initiatives to support Palestinian exporting companies. The project also aims to qualify and support 30 MSMEs, helping them gain the capacity to export.

Several trade agreements between Palestine and the EU have been implemented, including the Euro-Mediterranean Interim Association Agreement in 1997 and the Further Liberalization Agreement, enacted in 2012 for ten years and extended in 2021 for another decade.[38] These agreements were designed to enhance trade by providing duty-free access to EU markets for Palestinian industrial goods and agricultural products, while reducing tariffs on EU exports to Palestine. However, trade between Palestine and the EU remains limited due to movement restrictions and the overall economic situation. In 2022, Palestinian exports to the EU amounted to €25mn, primarily consisting of vegetal products (€17mn, 68%) and animal or vegetable fats and oils (€5mn, 20%).[39] In contrast, the EU imported €419mn worth of goods from Palestine, with transport equipment leading at €149mn (33.2%).

38 https://tinyurl.com/bdz5f6rk
39 Ibid

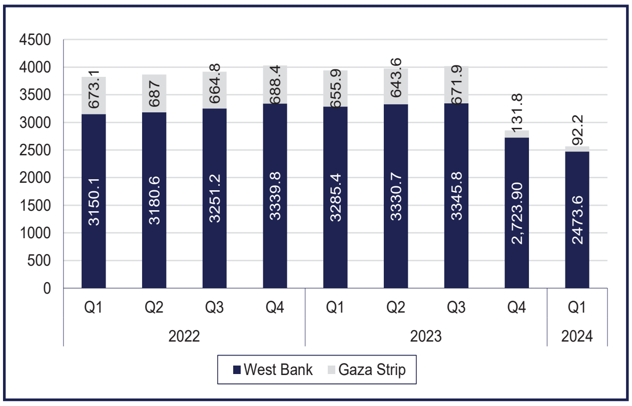
5. July Trading Activity

Al-Quds Index decreased by 3.1% in July 2024 compared to June 2023 and 21.0% compared to July 2023, reaching 508.6 points on the last trading day.[40] About 10.7mn shares worth $17.7mn were traded during the month, marking an 18.8% increase in the number and a 20.6% increase in the value of traded shares compared to June 2024.

40 https://tinyurl.com/yc7z64ut

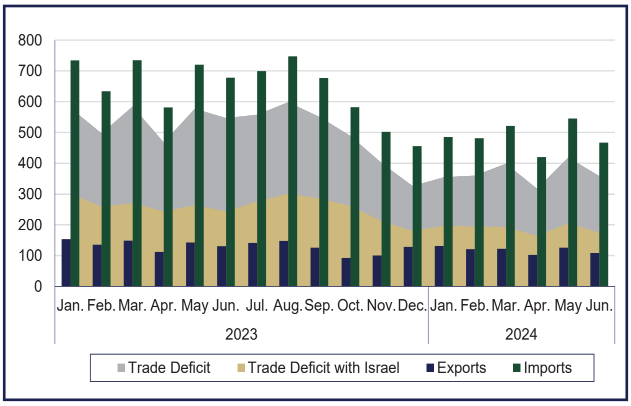
Gross Domestic Product

Quarterly Real GDP
(million USD in 2015 prices) in Palestine
by Region, Q1 2022 - Q1 2024



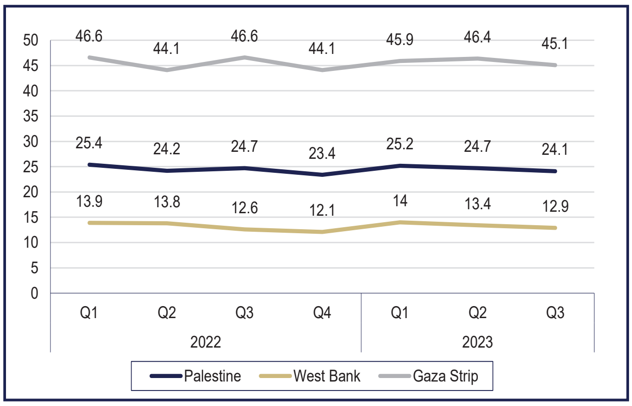
Trade

Monthly Export, Imports, Trade Deficit and Trade
Deficit with Israel (million USD) in Palestine,
January 2023 - June 2024



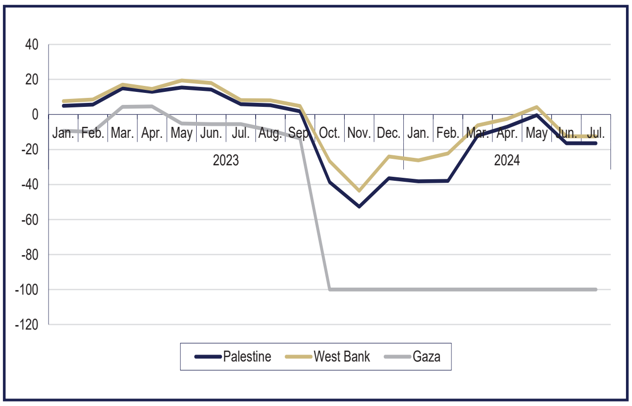
Unemployment

Quarterly Unemployment (%) in Palestine by
Region, Q1 2022 - Q3 2023



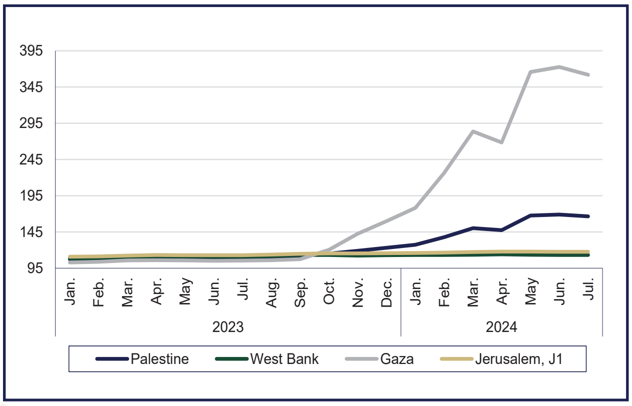
PMA Business Cycle Index

Monthly Palestine Monetary Authority
Business Cycle Index,
January 2023 - July 2024



Inflation

Monthly Consumer Price Index
(Base year = 2018) in Palestine by Region,
January 2023 - July 2024



Banking

Monthly Customer Deposits and Credit Facilities
(million USD) in Palestine,
January 2023 - June 2024