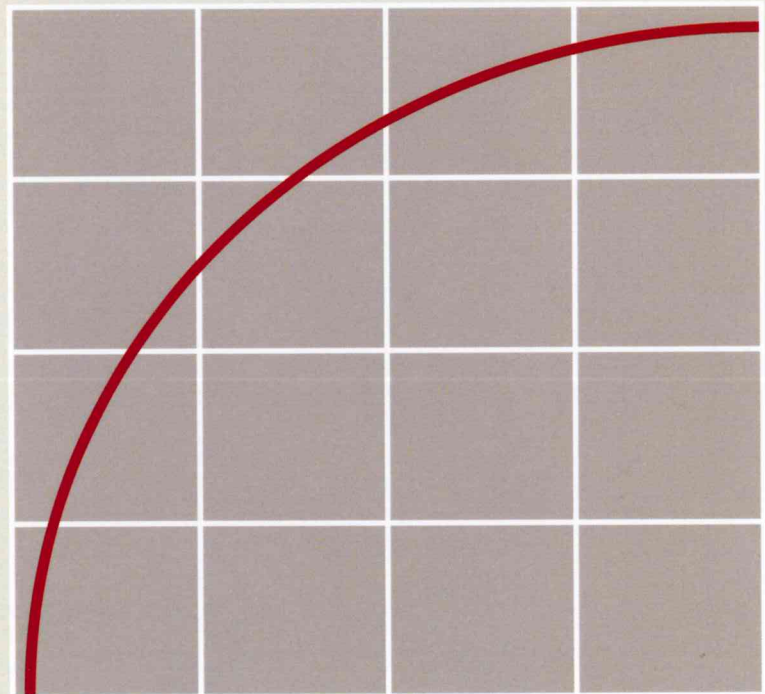


2010

Economic & Social Monitor

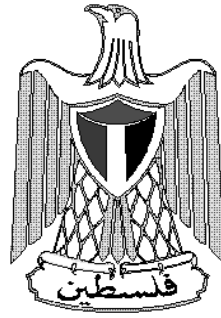


**Palestine Economic Policy Research Institute (MAS)
Palestinian Central Bureau of Statistics (PCBS)
Palestine Monetary Authority (PMA)**

**Volume 19
March**



**Palestine Monetary Authority
(PMA)**



**Palestinian Central Bureau of
Statistics (PCBS)**



**Palestine Economic Policy
Research Institute (MAS)**

***Quarterly*
Economic and Social Monitor**

Volume 19

March, 2010

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March, 2010

FOREWORD

This volume of the Economic and Social monitor outlines the main trends in economic and social development in the West Bank (WB) and Gaza Strip (GS) during the third quarter of 2009. These conditions are a continuation of what had been the case during the months of the second quarter of the year. At the political level, there has been no change in the political stalemate; the Israeli government continues to refuse to apply the terms of the road map. On the economic front, the Gaza Strip is still under siege and there has been no serious progress in addressing the catastrophic effects of Israeli attacks in the Gaza Strip (Dec. 27th, 2008 – Jan. 18th, 2009). As a result, economic activity continued to decline in Gaza and unemployment and poverty remain widespread. Economic activity in the West Bank also experienced a slight decline after the improvement that began at the end of last year as a result of the flow of international aid and the relative political calm that prevailed in the Palestinian territories in those months.

This volume contains estimated figures released by the PCBS regarding the total number of Palestinians living both within the Palestinian Territories and internationally at the end of 2009. It also includes three boxes addressing special issues. The first one deals with government priority interventions for 2010. The second box discusses the issue of food security in the Gaza Strip, while a third box discusses the issue of power in the Palestinian territories (PT), especially in relation to the Gaza Strip. In this volume, “*Economic Focus*” continues its discussion of economic growth, and deals specifically with the impact of foreign trade on economic growth.

We would like to reiterate our commitments to our readers and warmly welcome any feedback. We also wish to thank the teams at the three organizations that prepared this publication (PMA, PCBS and MAS).

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Executive Summary

Economic activity: Palestinian GDP witnessed an overall decrease of 4% in the 3rd quarter of 2009 compared with the 2nd quarter of the same year. Consequently, GDP per capita also decreased, by 1.1% for the same period, amounting to \$335.

Labor market: Unemployment increased by 16% in the 3rd quarter of 2009 compared with the 2nd quarter of the same year. This quarter witnessed an improvement in the participation rates of males in the Palestinian territories. As for the participation of females, rates declined in the West Bank by 7.5%; this is compared to the relative stability of the figure in the Gaza Strip. Average daily wages increased by 1% in the WB and decreased by 3% in the GS. Vacancies advertised in newspapers increased by 1.9% when compared to the previous quarter.

Public Finance: Government revenues totaled \$549.9 million in the 3rd quarter of 2009, with an increase of 54.3% compared to the previous quarter. 43.3% of this was from domestic revenues, amounting to approximately \$237.9 million. Total public expenditure increased by 53.4% to \$960.7 million compared to the previous quarter.

Banking developments: Credit facilities totaled \$2,261 million of total bank deposits during the 3rd quarter of 2009, with an increase of 35.4% compared to the previous quarter. In comparison with the previous quarter, bank assets increased in the 3rd quarter of 2009 by 5.2%, reaching \$8,156.5 million.

Palestine Securities Exchange: The Al-Quds (Jerusalem) index witnessed a decrease of 4.9% in the 3rd quarter of 2009 compared to the previous quarter. During the quarter, banks, industry and investment indices witnessed increases, while the indices of the insurance and services sectors decreased. 80.6 million shares were traded, with a value of \$50.8 million. The market value of listed companies amounted to \$2.23 billion.

Prices and purchasing power: The Consumer Price Index (CPI) in the PT increased during the 2nd quarter of 2009 compared to the previous quarter with prices increasing by 1.90%. It increased by 2.28% in the WB, while it increased by 2.04% in Jerusalem. In the same period, prices increased in the GS by 1.04%. The purchasing power of the US dollar and JD declined by 6.3% and 8% respectively.

Hotel Activity: At the end of the 3rd quarter of 2009, 120 hotels were operating in the West Bank and Gaza Strip. There were 135,939 visitors during the 3rd quarter of 2009, 14.7% of them were Palestinians while 34.4% of them were from the European Union, 50.6% of whom spent a night in Jerusalem.

Company Registration: The number of companies registered in the 3rd quarter 2009 decreased in the WB by 15% compared to the previous quarter to 349 companies. The capital for newly registered companies decreased also by 93%.

Building Licenses: The number of building licenses in the WB decreased during the 3rd quarter of 2009 by 18.2% compared to the equivalent quarter in 2008. The number of licensed dwellings in the WB increased by 11.7% compared to the equivalent quarter of 2008. Since the 1st quarter of 2008, there has been no available data for the GS. (Besides the 2nd quarter of 2008).

Industry Expectations: 19.2% of owners and managers of industrial firms in the WB and GS believed that their companies overall performance improved during September 2009 compared to the previous month. According to 78.8% of the owners and managers of industrial firms in the WB and GS, employment remained constant during September. In the medium term (the next six months), 26.2% of the owners and managers of industrial firms expected that the operational level in the WB and GS would improve.

Israeli Measures: During the 3rd quarter of 2009, 29 Palestinians were killed and 273 were injured. In the same period, crossing points between the WB and GS and Israel were fully closed 846 times and the number of temporary military checkpoints in the WB increased to 2,499.

Demographic reality: At the end of 2009, there were an estimated 10.88 million Palestinians in the world. The Palestinian territories are home to 36.7% of them, while

11.5% live in (Israel). 29.8% reside in Jordan, 16.3% reside in the rest of Arabic world and 5.7% of Palestinians live abroad in non-Arab countries. 2.48 million live in the WB and 1.52 million live in the GS.

Israeli attacks on the health sector: The numbers of direct Israeli attacks on ambulances were 3; 4 Paramedics were killed. There were 4 attacks on hospitals between bombings and military raids.

Key Economic Indicators in the West Bank and the Gaza Strip for the years 1994-2008

Indicator	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Population by mid 2009															
Palestinian Territories	-	-	-	2,871.60	2,962.20	-	3,053.30	3,138.50	3,225.20	3,314.50	3,407.40	3,508.10	3,612.00	3,719.20	3,825.50
West Bank	-	-	-	1,838.80	1,891.20	-	1,943.70	1,992.60	2,042.30	2,093.40	2,146.40	2,203.70	2,262.70	2,323.50	2,385.20
Gaza Strip	-	-	-	1,032.80	1,071.10	-	1,109.70	1,145.90	1,182.90	1,221.10	1,261.00	1,304.40	1,349.30	1,395.70	1,440.30
National Accounts															
GDP	3,012	3,193	3,286	3,702	4,148	4,512	4,119	3,765	3,264	3,750	4,198	4,560	4,322	4,536	4,640
GDP per capita (USD)**	1,406	1,388	1,348	1,438	1,558	1,640	1,450	1,288	1,085	1,211	1,317	1,387	1,275	1,298	1,290
Household Expenditure**	3,062	3,093	3,106	3,493	3,807	4,180	3,982	3,901	3,628	4,103	4,400	4,468	4,198	4,374	-
Gross Capital Formation**	1,052	1,065	1,161	1,311	1,531	2,081	1,561	1,120	954	1,204	1,022	1,266	1,347	1,310	-
Net Balance of Goods Trade**	1,609-	1,522-	1,652-	1,786-	1,951-	2,636-	2,432-	2,055-	2,082-	2,382-	2,210-	2,009-	1,669-	1,575-	-
Commodity Imports**	2,022	1,980	2,164	2,326	2,601	3,271	2,979	2,419	2,424	2,777	2,622	2,467	2,204	2,093	-
Commodity Exports**	413	458	512	540	651	635	547	363	342	394	412	458	535	518	-
Prices and Inflation															
Average Exchange Rate of the USD Against The Shekel	3.010	3.010	3.239	3.554	3.802	4.162	4.086	4.208	4.742	4.550	4.478	4.482	4.454	4.110	3.567
Average Exchange Rate of the JOD Against the Shekel	4.304	4.304	4.548	5.007	5.351	5.839	5.811	5.928	6.674	6.417	6.307	6.317	6.292	5.812	5.042
Inflation Rate (%)***	-	-	-	7.6	5.6	5.5	2.8	1.2	5.7	4.4	3.0	4.1	3.8	1.9	9.9
Labor Market															
Number of Employees (thousands)		417	429	481	549	588	600	505	477	564	578	633	622	666	648
Participation Rate (%)	-	39	40	40.5	41.4	41.6	41.5	38.7	38.1	40.3	40.4	40.7	41.3	41.9	41.3
Unemployment (%)	-	18.2	23.8	20.3	14.4	11.8	14.1	25.2	31.3	25.6	26.8	23.5	23.6	21.5	26

Indicator	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Social Conditions															
Poverty Rate (%) ****	-	-	23.6	22.5	20.3	-	-	27.9	-	-	25.6	29.5	30.8	34.5	-
Deep Poverty Rate (%) ****	-	-	14.3	14.2	12.5	-	-	19.5	-	-	16.4	18.1	18.5	23.8	-
Public Finance (Million USD)															
Net Domestic Revenues *****	-	-	-	807	868	942	939	273	290	747	1,050	1,370	722	1,616	1,780
Current Expenditures and Net Lending	-	-	-	862	838	937	1,199	1,095	994	1,240	1,528	1,994	1,426	2,567	3,273
Externally Supported Development Expenses	-	-	-	500	520	474	469	340	252	395	0	287	281	310	190
Surplus (deficit) Budget before Support	-	-	-	(55)	30	5	260-	(822)	(704)	(493)	(478)	(624)	(704)	(951)	(1,493)
Total Grants & Assistance	-	-	-	520	530	497	510	849	697	620	353	636	1,019	1,322	1,953
Total Surplus (deficit) Budget	-	-	-	35-	40	28	219-	313-	259-	268-	125-	275-	34	61	270
Public Debt	-	-	-	212	309	309	795	1,191	1,090	1,236	1,422	1,602	1,494	1,439	1,406
Banking Sector (Million USD)															
Assets/Liabilities	-	-	-	2,908	3,337	3,857	4,593	4,430	4,278	4,728	5,101	5,604	5,772	7,004	5,645
Equity	-	-	-	216	222	246	242	206	187	217	315	552	597	702	857
Client Deposits	-	-	-	2,090	2,415	2,875	3,508	3,398	3,432	3,625	3,946	4,190	4,216	5,118	5,847
Credit Facilities	-	-	-	578	777	967	1,280	1,186	942	1,061	1,417	1,788	1,843	1,705	1,829
Number of Banks	7	13	15	19	21	21	21	21	20	20	20	20	21	21	21

Source: Central Bureau of Statistics, the Palestinian Monetary Authority.

* West Bank: means the West Bank except that part of the Jerusalem governorate which was annexed forcefully by Israel following its occupation of the West Bank in 1967.

** Data in constant prices. Base year for the 1994-2003 is 1997; base year for 2004-2008 is 2004. Data for 2008 is preliminary and subject to revision and amendment and is based on quarterly estimates.

*** According to the inflation rate based on the comparison of average indices of consumer prices for the comparison year with its average in the previous year. Base year for the period 1994-2006 was 1996 (1996=100), base year for 2007 and 2008 is 2004 (2004=100).

**** The PCBS defines poverty in relation with the family budget Deep Poverty any standard family (6 members: two adults and 4 children) possessing a budget that is less than NIS 1,886 monthly (2007) to cover for the expenses of food, clothing and housing. Relative poverty: any standard family (6 members: 2 adults and 4 children) possessing a budget less than NIS 2,362 monthly to cover the expenses of food, clothing, housing, health, education, transportation and other expenses.

***** The total net income is the total current income after the deduction of tax returns.

- Figures in brackets are negative.

1. The Monitor Outlook

The political and economic developments that occurred in the 3rd quarter of 2009 were a continuation to those of the first and second quarters. The Palestinian internal relations crisis continued despite the Egyptian and Saudi attempts to reach a national reconciliation among Palestinian factions and regain the Palestinian unity. Moreover, the Israeli government continued its obstinacy and refusal to comply with the conditions of the road map to stop Jewish settlement activities in the West Bank, paving the way to resume the negotiations with the Palestinians. On the contrary, the settlement activities increased particularly in Jerusalem and its suburbs. This activity was also coupled with the application of a package of policies by the Jerusalem municipality aiming at reducing the number of Arabs to the minimum possible in order to have complete control over the city; thus creating additional obstacles in the way to launch the negotiations on issues for final solution. This obstinate Israeli position is encouraged by the American aptitude to back off when confronted by Israeli opposition, as long as the international community follows the American lead. Also, the Israeli siege on the Gaza Strip continued together with the freezing of reconstruction of the destruction caused by the recent Israeli aggression. The Gaza Strip people's suffering continued with most of them living under extremely stringent conditions this winter.

In this context, it must be noted that this political impasse in the negotiations between the Palestinian Authority and Israel is not new. Since the failure of the Camp David negotiations between the two parties in 2000, the relations between them have been critical and no progress has resulted from the many recurring meetings held during the last ten years. We should also realize that this impasse in the negotiations between the two parties does not mean that the political and economic conditions are stagnant on the ground. On the contrary, they are naturally evolving all the time. Obviously, this development has resulted in the establishment of two contradictory situations.

The first situation is represented in an unprecedented international consensus of adopting 'the two states solution' to end the Palestinian–Israeli conflict. The world powers and the United Nations have adopted this solution in 'the road map'. The Arab League adopted this solution in the 'Arab Peace Initiative' and even Israel did not oppose to a Palestinian state as it usually did in the past.

The second situation is represented in the Israeli practices in the West Bank described by many observers as attempts to undermine any possibility of building a Palestinian state within the 'two state' scope. This explains why many observers consider that the 'two state' solution is not practical and it also explains the growing talk in the political and academic realm about the 'bi-national state' solution.

Perhaps, the best analysis of this was conducted by Merno Benvensti.¹ He examined the meaning and significance of this contradiction between the declared Israeli and international positions regarding the 'two states' solution and what is occurring on the ground in the systematic and consistent practices to undermine the foundations of such a solution. In his important article in Haaretz on the 22nd January, 2010, Benvensti explained the above mentioned apparent contradiction.

Benvensti refuses the use of 'the occupier/occupied paradigm' for the analysis of the ongoing conflict in Palestine as this model is based on three assumptions that facts on the grounds have proved are incorrect:

The first hypothesis assumes that the relationship between the Palestinians and the Israelis in its current state emerged after the Israeli occupation of the West Bank and the Gaza Strip in the 1967 war and that this situation will change as soon as the two parties reach an agreement to end the conflict. On the contrary, Benvensti sees that the situation which emerged after the 1967 war is a return to the 'constant' situation between the two parties. A situation that began at the start

¹ Benvensti is the preceding deputy Mayor of Jerusalem and the most prominent expert in Palestinian – Israeli relations.

of the Zionist project at the end of the 19th century and that the 'temporary' situation is that which prevailed for the period of 19 years between 1948 and 1967, not that which followed.

The second hypothesis assumes that the building of Jewish settlements on the Palestinian lands in the West Bank is currently the most important obstacle that hinders the solution between the two parties in the framework of the 'two states' solution. Benvensti considers that the main obstacle lies in the overall practices of the Israeli system which works relentlessly to weaken the Palestinians and to separate their lands. He also believes that the Israeli settlements reached, at some time in the eighties, the point of no return. This means that after this date the number of settlements and settlers does not matter, as the growth of the settlements has been materially established and there is no difference between the areas of settlements in the West Bank and parts of Israel.

The third assumption says that the peace camp in Israel has won the battle against the right wing when the latter dumped the goal of 'greater Israel' and accepted the establishment of the Palestinian State within the framework of the 'two state' solution. The author thinks that the *right* did not change its position at all, but has verbally accepted the Palestinian state after the change of the conditions on the ground, and when the establishment of a Palestinian state meant no more than a limited self rule that is not much different than Menahem Begin's concept presented during the Camp David negotiations with Anwar Sadat in 1979. The Palestinian state that is currently accepted by Israel is a group of municipalities that has no connected infrastructure and no control over its airspace, water resources or on its borders with the outside world. In other words, it is 'a state without a head or feet and no chance of progress'. The borders of such a state are the 'length of its buildings and the depth of its graves', as he says.

The author thinks that what is actually going on at ground level is a systematic arrangement of maintaining the status quo, which he calls a 'dual nationality' system. It is worth noting that Benvensti does not believe that this

system will lead to a 'De-facto bi-national regime' where the Palestinians enjoy their national rights, as this is suicidal for Israel. It is believed that the system created on the ground by Israel and which is liable to continue is the continuation of the status quo with all the oppression it entails for the Palestinian people. Unlike many observers, the author believes that this situation is neither 'temporary' nor 'chaotic' but is given a great force for continuity. He also believes that one of the important factors that help the continuity of the status quo is the Palestinian divide into five separate entities with near to political and economic diverging interests. These are 1) the population of the West Bank 2) the population of East Jerusalem 3) the population of the Gaza Strip 4) the Palestinians who hold the Israeli citizenship 5) Palestinian refugees in the world. He thinks that the main tool used by Israel to maintain the 'temporary' is the feeding of differences among these entities according to the policy of 'divide to rule'. He points that the policy of dividing Palestine into separate entities with different interests explains why the Israeli rightists do not fear the 'demographic bomb' released by the Zionist left.

In addition to the division of Palestinians into five entities, Benvensti believes that there are another five factors that help Israel to continue with the status quo. They are: a) the success of successive Israeli governments in mobilizing the Israeli community in support of the occupation as a defense of Israeli existence; b) the donor countries continuing to finance the persistence of the status quo; c) the practices of the Arab countries that are based on bilateral agreements and international relations rather than the Arab national interests and the belief of some Arab regimes that the continuation of the status quo is better for their interests than the establishment of a Palestinian state; d) Israel's success in giving the impression that the negotiations with the Palestinians means that the current situation is temporary; e) Israel's success in silencing the critics of its policies against the Palestinians by linking these policies with the claims of fighting international terrorism.

Benvensti's beliefs may not reflect the reality as it is. His predictions may not be right but the reader of his article will surely feel that he

made a serious attempt to see the whole picture and not one part only. The Palestinian reader will certainly feel that the Palestinian internal divide in the past years has imprisoned him for a long period among single trees so that he can no longer see the forest. That is why there is a need to discuss the hypotheses and opinions of this article in order to achieve an in-depth understanding of the stage we are passing through and the roles of various powers. The results of such a discussion may serve the expedition of a serious and constructive political dialogue among various Palestinian political factions to end the political divide as soon as possible. It may also form a national salvation and consensus government to undertake the burdens of reform and development as well as the plan for the reconstruction of the Gaza Strip and the plan for building the institutions and foundations of the Palestinian state with an aim to:

- ✧ End the siege on the Gaza Strip, start the rebuilding and reconstruction process, lessen the sufferings of the citizens and launching the process for development.
- ✧ Reconnect the West Bank and the Gaza Strip economically and at the same time

link the relief process in the Palestinian Territories in the short run with the national plan for development and continue the efforts for linking international aid with the plan for development.

- ✧ Face the economic and social policy for the marginalization of Jerusalem by supporting economic and cultural activities in Jerusalem and by confronting the attempts to detach the city from its surrounding and disintegrate its economic ties with other governorates.
- ✧ Allocate more financial resources for the implementation of the strategy of 'pro-poor growth' particularly in marginalized areas behind the Wall, in the Jordan Valley and rural outskirts, by providing educational and health services together with policies and measures that help the poor and marginalized to participate in the economic, political and social life.
- ✧ Initiate economic policies that will give the private sector potential to overcome the depressive factors in the investment environment that was caused by the aggression, destruction and instability in the region.

2. Economic Activities

The 3rd quarter of 2009 witnessed a slight decline in macroeconomic indicators compared to the 2nd quarter of the year. The unemployment rate registered an increase of 16% in the 3rd quarter compared to the 2nd quarter and the real GDP per capita declined by 1.1% between the two quarters as well. This decline follows the recovery that occurred in the first half of the year which led to disappointment regarding the growth in the economic activities in the year 2009, accompanied with an increase in the employment rates. The decline in the 3rd quarter is accompanied with the fragile nature of economic recovery that occurred during the period 2007-2008 which is characterized by the following:

✧ The economic recovery that the Palestinian Territories witnessed recently is due to the relative recovery of the economic activity in the West Bank; while the economic activity in the Gaza Strip is still suffering from recession and deterioration. Looking at the unemployment rates in the Palestinian Territories in the 3rd quarter of 2009, it is realized that it amounted to 42.3% in the Gaza Strip (more than double the rates in

the West Bank, 17.6%) which could be the highest in the world. The reason for this is mainly the restrictive siege imposed by Israel on the Gaza Strip paralyzing all aspects of economic activity. It is noted that while the construction sector absorbs 16% of the total labor force in the West Bank, this sector employs less than 1% of the total labor force because of the prevention on entering construction materials into the Gaza Strip. The same applies to the mining and industry sector which employs about 14% of the total labor force in the West Bank versus 0.6% only in the Gaza Strip.

✧ The economic activity in the West Bank depends mainly on the financial aid of donor countries, which mostly goes to the support of the Authority budget. The size of aid and grants was equivalent to 53.6% of the GDP in the 3rd quarter of 2009 which was mostly used to support the current public expenditure (salaries and wages); while the development expenditure did not receive more than 3.3% of the total aid extended during the first three quarters of 2009.

Table 1: Economic Growth and Unemployment for the 3rd Quarter of 2008 and the 3rd Quarter of 2009

Indicator	3 rd Q* 2008	4 th Q* 2008	1 st Q* 2009	2 nd Q** 2009	3 rd Q*** 2009
GDP in constant prices (million USD)	1,180.2	1,145.0	1,177.3	1,249.7	1,244.8
GDP per capita (USD)	326.9	314.9	321.4	338.8	335.0
Per capita Growth Rate (%)	(1.4)	(3.7)	2.1	5.4	(1.1)
Unemployment Rate (%)	27.5	27.9	25.4	22.2	25.8

Source: PCBS, 2009, National Accounts Statistics, Ramallah – Palestine.

* Preliminary data subject to revision and amendment.

** First revision, preliminary and subject to revision and amendment.

*** Preliminary estimates (first version), subject to revision and amendment.

- Figures are in constant prices for the West Bank and Gaza Strip and the base year is 2004.

- Numbers in brackets indicate negative value.

It is expected that the fragile conditions of the economic activity will continue unless a radical change happens in the whole political situation, for example the end of the Israeli siege on the Gaza Strip and the end of Israeli oppressive measures, practiced in the West Bank since 1967. As it is known, the Israeli

measures succeeded in making the Palestinian economy dependent on external sources of income (income of workers in Israel and the settlements and the income of workers in the Gulf countries). The Palestinian economy also suffers from serious distortions exemplified in the control of Israel on a considerable part of

the natural resources (land and water); and from sectoral imbalances (the very low participation of agriculture and industry in the GDP), and the complete dependency on Israel for imports and exports, in addition to a great drop in the level of productive investment and social services. The result was that the Palestinian economy suffers from many distortions and imbalances that can be summarized as follows:

❖ **Sectoral disarticulation**

The proportion of the productive sectors contribution to the GDP is very

low. In 2008, the contribution of agriculture and industry was 18.2% of the GDP and 17% by the end of the 3rd quarter of 2009. It is worth noting that with regard to agriculture and manufacturing in particular, these proportions dropped to 13.8% and 13.2% in 2008 and the 3rd quarter of 2009, respectively. These proportions are much lower than the levels of countries with economies similar to the Palestinian economy in terms of standards of living (see tables 2 & 5).

Table 2: Percentage Contribution of Agriculture and Industry to the Gross Domestic Product

	(Percentage)		
	1995	2003	2008
Palestine	33.2	33.2	17.5
Average of lower middle income countries	-	58.0	-

Source: World Bank Development Report 2004, 2009.

❖ **Resource Gap²**

The Palestinian economy suffers chronically from a resource gap reflected in a substantial deficit in the balance of trade in merchandise (merchandise imports – merchandise exports). The value of exports covers less than one fourth of the value of imports. The deficit makes up for more than one third of the GDP. The other side of the resource gap is, of course, the existing deficit between the volume of domestic savings and the expenditure of investments (investment - savings). The volume of domestic savings is of negative value in the Palestinian economy, and was equivalent in 2007 to nearly 15% of the GDP.

❖ **Labor Market Imbalance**

The Palestinian economy suffers from a state of chronic imbalance in the labor market. Domestic economic activity absorbs less than 66.3% of the labor force while about 7.9% are employed in the Israeli economy. The rate of

unemployment reached nearly a quarter of the labor force.

The harming effects of such deformations become evident when comparing the income of the Palestinian individual to the average income of an individual in neighboring countries. While the average income of a Palestinian individual was slightly higher than the income of an Egyptian individual in 2000, it became equivalent to less than three quarters of that income in 2007. Also, the average income of a Palestinian individual was equivalent to more than 164% of the average income of an individual in Syria in 2000, but it became equal to 69% of the income of an individual in Syria in 2007 (see table 4).

It should not be assumed that the difficulties encountered by the Palestinian economy in the West Bank and the Gaza Strip are due only to accumulations caused by the setbacks during the last eight years. In reality, the events of those years clearly reveal the fragility of the economy's structure and the deformations and imbalances present in all its aspects. This is a natural result of the restrictions imposed by the Israeli authorities during four decades of occupation. It is known that those policies succeeded in making the Palestinian economy

² Domestic savings is calculated as GDP minus total household consumption expenditures and governmental consumption expenditures from the GDP (saving = GDP – (private consumption + public consumption). The resource gap may be seen either as the difference between the size of exports and imports or as the difference between domestic savings and the size of investments.

an economy mainly dependant on external sources of income (income of workers employed in Israel and the settlements and income of those employed in the Gulf countries). It also suffers from serious deformations represented by Israel's control over an important part of natural resources (land and water). Those policies also succeeded in making the Palestinian economy suffer from sectoral imbalances (extremely

low contribution of agriculture and industry to GDP), total dependence on Israel for export and import, and extremely low levels of productive investments and of social services. To understand the nature of the present difficult financial situation it has become necessary to re-examine the successive political-economic developments that the Palestinian scene has witnessed.

Table 3: Main Economic Indicators in the West Bank and the Gaza Strip* 3rd Quarter 2008 and 3rd Quarter 2009

Indicator	(USD Million)				
	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009
GDP in constant prices**	1,180.2	1,145.0	1,177.3	1,249.7	1,244.8
GDP per capita in constant prices**	326.9	314.9	321.4	338.8	335.0
Participation in the labor Force (%)	41.6	41.4	41.4	41.7	41.6
Unemployment rate (%)	27.5	27.9	25.4	22.2	25.8
Inflation rate (%) ***	1.83	0.20	(1.01)	0.86	1.90
Total net revenues	554.8	302.9	334.9	355.7	450.9
Public expenditures	1,064.0	618	712.4	626.2	960.7
Surplus/Deficit before support	(509.0)	(315.2)	(388.6)	(318.5)	(575.7)
Surplus/Deficit after support	(33)	36	(110.3)	(157.5)	92.7
Actual external assistance	476.1	351	278.3	161.8	667.7
Bank Deposits by residents	5,873.6	5,846.9	772.5,5	5988.7	6385.9
Credit facilities	1,807.5	2,81,82	842.9,1	2099.7	2261.2

Source: The Palestinian Central Bureau of Statistics - PCBS (National Accounts Statistics, Price Indices), Palestine Monetary Authority-PMA (Public Finance Indicators, Banking Indicators).

* The remaining West Bank is the West Bank excluding that part of the Jerusalem governorate that was annexed by Israel following Israel's occupation of the West Bank in 1967.

** Figures are in constant prices for the remaining of the West Bank and Gaza Strip and the base year is 2004 and these figures are preliminary and subject to modification.

*** Inflation rate was calculated by comparing the average consumer prices for a given quarter with the average of the previous quarter. The base year for the CPI is 2004 (2004=100) given that the West Bank figures include East Jerusalem.

- Numbers in brackets indicate negative value.

Table 4: The Ratio of the Average Palestinian Income /Capita compared to its Level in Neighboring Countries (%)*

Country	2000	2005	2007**
Egypt	108	97	78
Jordan	88	49	43
Syria	164	86	69
Lebanon	35	22	21
Israel	8.8	6.2	5.6

Source: These ratios were calculated based on data from 'World Development Indicators (2008).

* The average income per capita is represented by the country's Gross National Income (GNI) per capita.

** Based on the assumption that the GNI per capita in the West Bank and the Gaza Strip in 2007 is equivalent to its level in 2005 (taking into account that the income in 2007 was probably less than that of 2005).

As for the contribution of the different economic sectors to the GDP, the 3rd quarter of 2009 witnessed a slight rise in the contribution of industry, wholesale and retail

trade, transportation, storage and telecommunication sectors in the GDP, compared to a decline in the contribution of the agriculture sector (see table 6).

Table 5: The Contribution of Economic Activities in the GDP in the Remaining West Bank* and the Gaza Strip for the 3rd Quarter of 2008 to the 3rd Quarter of 2009 in Constant Prices: base year 2004 (%)

Economic Activity	2008		2009		
	3 rd Quarter**	4 th Quarter**	1 st Quarter**	2 nd Quarter***	3 rd Quarter**
Agriculture and Fishing	4.2	4.4	3.6	4.0	3.3
Mining, Manufacturing, Water and Electricity Supplies	13.4	14.1	14.0	13.5	13.7
Mining and quarrying	0.3	0.3	0.4	0.3	0.3
Manufacturing	9.7	10.2	10.0	9.8	9.9
Water and Electric Supplies	3.4	3.6	3.6	3.4	3.5
Construction	4.6	5.0	5.3	6.2	5.7
Retail and Wholesale	10.7	11.2	10.5	10.0	10.3
Transportation, storage and telecommunication	9.4	9.0	9.4	9.1	9.4
Financial intermediation	5.4	5.8	5.7	5.6	5.7
Services	24.4	26.2	26.2	26.6	26.1
Real estate, rental and commercial activities	8.5	9.1	10.0	10.0	9.2
Communal, social, and personal activities	1.5	1.5	1.8	1.9	1.9
Hotels and restaurants	1.9	2.5	1.4	2.1	2.5
Education	9.6	10.2	10.1	9.7	9.6
Health and social work	2.9	2.9	2.9	2.9	2.9
Public administration and defense	13.7	13.3	14.1	13.9	13.8
Domestic services	0.1	0.1	0.1	0.1	0.1
Subtract: financial intermediation (with indirect clearing)	-5.7	-5.8	-5.2	-5.2	-5.4
Add: Customs fees	6.9	6.2	6.3	6.4	6.7
Add: Net VAT on imports	12.9	10.5	10.0	9.8	10.6
GDP (%)	100	100	100	100	100
GDP	1,180.2	1,145.0	1,177.3	1,249.7	1,244.8

Source: PCBS, 2009. Press Release on preliminary estimates of the 'Quarterly National Accounts Statistics', (3rd quarter 2009), Ramallah – Palestine.

The contribution of the publicly-owned enterprises to the GDP has been distributed on retail & wholesale, real estate, rental, commercial, education, restaurant and hotel activities.

* The remaining West Bank is the West Bank excluding that part of the Jerusalem governorate that was annexed by Israel following Israel occupation of the West Bank in 1967.

** Figures are preliminary and subject to revision and modification.

*** First revision: preliminary and subject to revision and modification.

**** Preliminary estimates (first issue): subject to revision and modification.

BOX 1: Government Intervention Priorities for 2010

In cooperation with other ministries and government bodies, the Ministry of Finance and the Ministry of Planning and Administrative Development issued the document 'Palestine: the Way Forward'. This document presents a list of priority projects that the Palestinian Authority intends to carry out during 2010 and subsequent years. The priorities identified are consistent with the document 'Palestine: ending the occupation and building the state' declared by the thirteenth Government as a program and plan of action to meet the requirements of establishing an independent state in two years time.

The intervention plan casts light on 201 development projects categorized as a priority to be implemented during 2010 and subsequent years. The total estimated cost for the implementation of these projects amounts to USD 5.5 billion, of which USD 667 million is planned to be spent during the year 2010, in accordance with the Reform and Development Plan 2008-2010. The plan indicates that some projects are earmarked and underway, while others are not funded or partially funded. The following table demonstrates a summary of the plan:

Main Objectives	Number Of Projects	Expected Cost (USD Thousand)	Percentage of Total Cost (%)
Finalize the building of central and local government institutions, indispensable for the establishment of a modern Palestinian State with sovereignty on June 1967 borders	42	582,724	11%
Raise the level of public services provided to all citizens in all parts of the Palestinian Territories occupied in 1967	68	1,219,949	22%
Launch large projects to build the infrastructure in all parts of the Palestinian Territories occupied in 1967	88	3,702,567	67%
Improve and enhance the image of Palestine internationally and its role in achieving stability and prosperity in the region	3	31,399	1%
Total	201	5,536,638	100%
The Case	Number of Projects	Expected Cost (USD Thousand)	Percentage of Total Cost (%)
Funded projects underway	50	1,376,944	25%
Partially funded projects	4	102,001	2%
Pledged projects	14	1,256,580	23%
Unfunded projects	133	2,801,113	51%
Total	201	5,536,639	100%

The table illustrates that 54 of these projects, which total 27% of the total estimated cost, have actually begun, or are at least partially funded projects. So far, 14 other projects, constituting 23% of the total estimated cost, are pledged.

Most of the projects included in the Plan are infrastructure projects (27%) comprising of the construction of facilities for sewage treatment, building desalination plants, prisons, railway networks and a commercial port, in addition to the building of at least one airport. It is expected that most projects will take several years to be completed, particularly the infrastructure projects.

3. Labor Market

The key indicators that determine the number of workers in the economy are three: the number of the working-age population, the rate of participation in the labor market and the unemployment rate; while the role of workers in the economic activity is determined by indicators pertaining to the human capital. These include the volume of physical capital available for workers and the nature of the institutions that have a direct or indirect impact on the production process. The Palestinian labor market reflects the economic conditions in general. On the quantitative level, we notice a rise in the level of the working-age population, a decline in the rate of labor force participation and a rise in unemployment rates. The labor market suffers from imbalances, demonstrated in the inability of the demand level to meet the level of supply. When closely examining the causes of this inability, we find that the main cause lies in the drop in the size of the general demand for goods and services (consumption, investment, public expenditure and exportation). Specifically in the weakness of investment activity and its inability to create sufficient capital accumulation to generate sufficient job opportunities capable of absorbing the annual increase in the labor force.

This imbalance was exacerbated during the Intifada because of the considerable shrinking of the economic activity as a result of the Israeli army practices. These included killing, destruction, siege and closures, the building of the expansion and annexation wall and the restrictions imposed on the mobility of persons and goods between the West Bank and the Gaza Strip as well as between towns and villages within the respective regions. During the years of the Intifada, the annual increase in manpower was higher than the increase in the labor force (3.6% annual increase in manpower and 3.5% annual increase in the labor force). This indicates that labor force participation was declining. This indicates a decline in the labor participation rate, which actually declined by 0.1% a year. The average increase in the labor force (3.5%) was also higher than the average increase in employment (1.1%), indicating that the unemployment rate was rising with an average

annual increase of 13.4%. Moreover, the employment in the public sector increased slightly over the employment in the private sector.

3.1 Labor Force and Labor Force Participation

Quarterly data registered a decline in the number of those employed. The number dropped from 738.7 thousand workers in the 2nd quarter of 2009 to 709.2 thousand workers by the end of the 3rd quarter of the same year. At the same time, the average labor force participation rate (LFPR) witnessed a slight rise in the first 3 quarters of 2009 as compared to its level in the corresponding quarters of 2008 (see table 6).

With regard to participation rate by region, the disparity between the West Bank and the Gaza Strip persisted. This was intensified during the Intifada years due to the imposed strict siege on the Gaza Strip. The labor force participation rate amounted to 43.7% in the West Bank by the end of the 3rd quarter of 2009, while it did not exceed 37.7% in the Gaza Strip.

The 3rd quarter of 2009 witnessed an improvement in the labor force participation rates of males in the Palestinian Territories, rising from 66.7% in the 2nd quarter to 67.2% in the 3rd quarter of 2009. This rise is attributed to the slight rise in the labor force participation rates of males in the Gaza Strip after five months of the of the Israeli aggression on the Gaza Strip, while the LFPR of males remained relatively stable in the West Bank. As for the LFPR of women, in spite of the improved levels during the past few years caused by women increasingly entering the labor market to compensate for the lost income of their male relatives, these rates deteriorated in the West Bank and remained relatively stable in the Gaza Strip in the 3rd quarter of 2009.

As for workers' employment status, the quarterly data indicates a rise in the percentage of those employed in establishments they own or partially own, in addition to a rise in waged workers and a drop in the percentage of unpaid

workers. The increase in the percentage of those working in establishments they own or partially own indicates, as was the case since the beginning of the *Intifada*, that a

considerable percentage of those who lost their work in Israel or in the private sector after the *Intifada* tended to be self-employed.

Table 6: Labor Force Participation Rate for Individuals Aged 15 Years and Over in the Palestinian Territories According to Place of Work and Sex: 2008 Quarters and the First 3 Quarters of 2009

Region and Sex	(%)						
	1 st Q 2008	2 nd Q 2008	3 rd Q 2008	4 th Q 2008	1 st Q 2009	2 nd Q 2009	3 rd Q 2009
Both Sexes							
West Bank	42.3	43.5	43.4	42.8	42.8	44.4	43.7
Gaza Strip	37.5	38.0	38.2	38.8	38.9	36.9	37.7
Palestinian Territories	40.6	41.6	41.6	41.4	41.4	41.7	41.6
Males							
West Bank	67.5	68.0	69.4	68.3	68.5	69.6	69.5
Gaza Strip	63.3	63.2	64.0	65.4	63.8	61.4	63.1
Palestinian Territories	66.0	66.3	67.5	67.3	66.9	66.7	67.2
Females							
West Bank	16.5	18.2	16.9	16.7	16.5	18.7	17.3
Gaza Strip	11.3	12.0	11.9	11.7	13.5	11.8	11.9
Palestinian Territories	14.7	16.0	15.2	15.0	15.4	16.2	15.4

Source: PCBS (2009), Labor Force Survey, 2008-2009.

Table 7: Percentage Distribution of the Employed Persons in the Palestinian Territories According to Employment Status, and Region 2008 Quarters and the First 3 Quarters of 2009

Region and Work Status	(%)						
	1 st Q 2008	2 nd Q 2008	3 rd Q 2008	4 th Q 2008	1 st Q 2009	2 nd Q 2009	3 rd Q 2009
West Bank							
Employer	4.2	4.3	4.5	5.0	6.0	7.0	7.5
Self-employed	22.9	24.1	22.8	16.4	20.8	19.8	20.2
Wage employee	64.2	60.4	62.2	67.9	64.6	62.5	63.1
Unpaid family member	8.7	11.2	10.5	10.7	8.6	10.7	9.2
Gaza Strip							
Employer	2.9	3.3	4.6	3.5	5.3	3.9	3.6
Self-employed	27.3	16.9	15.7	12.0	14.9	13.2	15.4
Wage employee	58.5	71.3	73.3	79.0	73.7	79.5	78.2
Unpaid family member	11.3	8.5	6.4	5.5	6.1	3.4	2.8
Palestinian Territories							
Employer	3.8	4.0	4.5	4.6	5.8	6.2	6.5
Self-employed	24.3	22.4	21.0	15.3	19.1	18.0	19.0
Wage employee	62.5	63.0	65.1	70.7	67.2	66.9	66.9
Unpaid family member	9.4	10.6	9.4	9.4	7.9	8.9	7.6

Source: PCBS (2009), Labor Force Survey, 2008-2009

Quarterly data indicates a change in the percentage distribution of employed persons

by economic activity. The 3rd quarter of 2009 witnessed a rise in the percentage of workers

in the industry sector compared to a decline in the agriculture and services sectors and relative stability in the construction sector (see table 8). The slight decline in the services sector does not negate the fact that the general trend is a rise in this sector, amounting to 39.4% by the end of the 3rd quarter of 2009, where the percentage of workers in the services sector increased during the years of the Intifada in particular. Those years are also

characterized by an increase in the percentage of workers in the agricultural sector, but to a lesser degree. This is compared to a decline in the percentage of workers in the construction sector to about half its level prior to the Intifada due to the prevention of Palestinian workers, most of whom work in the construction sector, from working in Israel. The percentage of workers in mining, quarrying and manufacturing declined as well.

Table 8: Distribution of Employed Persons in the Palestinian Territories According to Region and Economic Activity, 2008 Quarters and the First 3 Quarters of 2009

Economic Activity and Region	2008 Quarters and the First 3 Quarters of 2009 (%)						
	1 st Q 2008	2 nd Q 2008	3 rd Q 2008	4 th Q 2008	1 st Q 2009	2 nd Q 2009	3 rd Q 2009
Palestinian Territories							
Agriculture, Forestry, Hunting & Fishing	12.9	14.9	12.7	13.0	11.7	12.3	10.7
Mining, quarrying and manufacturing	13.0	12.1	12.4	11.1	12.6	11.4	11.8
Construction	9.4	10.8	12.7	10.8	11.1	12.3	12.2
Services and other sectors	38.5	38.2	37.2	39.4	40.5	40.4	39.4
West Bank							
Agriculture, Forestry, Hunting & Fishing	13.0	15.7	13.5	15.0	13.1	14.9	12.6
Mining, quarrying and manufacturing	16.2	14.5	15.0	13.9	15.4	13.9	13.8
Construction	12.7	14.1	16.8	14.2	15.1	16.5	16.0
Services and other sectors	32.8	30.9	29.1	29.8	31.6	30.9	31.5
Gaza Strip							
Agriculture, Forestry, Hunting & Fishing	12.5	12.3	10.6	7.1	8.4	4.8	4.9
Mining, quarrying and manufacturing	5.5	4.6	4.8	2.7	5.6	4.2	6.0
Construction	1.6	0.4	0.7	0.8	1.0	0.7	0.9
Services and other sectors	52.0	61.4	60.7	67.9	16.9	67.0	63.2

Source: PCBS (2009), Labor Force Survey, 2008-2009

The percentage of workers in the West Bank amounted to 63.9% by the end of the 3rd quarter of 2009 compared to 25.4% in the Gaza Strip and 10.7% in Israel and the settlements. The 3rd quarter of 2009 witnessed a decline in the percentage of workers in the Gaza Strip compared to a rise in the percentage of workers in the West Bank, Israel and the settlements. The increase in the number of workers was very close in each of the West Bank and the Gaza Strip during the first three quarters of 2009, reaching about 5.6% for each (see table 9). These ratios are in

contrast with what was prevalent in the first year of closure of the Israeli labor market during the Al-Aqsa Intifada, which witnessed a larger increase in the number of workers in the West Bank than in the Gaza Strip. Data shows that the West Bank share of the total workers in the Palestinian Territories had increased in 2008 by 18% compared to its *pre-Intifada* level, while the Gaza Strip share did not exceed 8%. This indicates that the labor market absorption capacity for workers who lost their work in Israel during the Intifada was larger in the West Bank than in the Gaza Strip.

Table 9: Percentage Distribution of workers Aged 15 Years and Over in the Occupied Palestinian Territories according to Place of work, 2008 Quarters and the First 3 Quarters of 2009

Workplace	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009
Labor Force (thousand)	2,169.1	2,190.3	2,211.7	2,233.4	2,255.1	2,276.8	2,298.6
Number of Workers (thousand)	675.8	666.7	665.4	664.2	697.1	738.7	709.2
West Bank	59.0	65.3	62.4	62.9	61.6	63.7	63.9
Gaza Strip	29.8	23.9	25.5	25.0	28.4	26.1	25.4
Israel and settlements	11.2	10.8	12.1	12.1	10.0	10.2	10.7

Source: Palestinian Central Bureau of Statistics, 2009, Labor Force Survey 2008-2009.

3.2 Unemployment

The problem of unemployment is not new to the Palestinian economy, although its rates were much lower prior to the Al-Aqsa Intifada, but it has always been relatively high. Unemployment witnessed an increase from the 1st quarter of 2008 until the 4th quarter of the same year. When the rate of unemployment in 2008 is compared with its level prior to the Intifada, we realize that it soared up to more

than double. In 2008, the problem of unemployment increased dramatically in the Gaza Strip in particular, as a result of the Israeli siege and amounted to 44.8% in the 4th quarter of year, which was the highest in the world. Table 10 below illustrates a decrease in the rates of unemployment in the first 3 quarters of 2009 compared to 2008 quarters.

Table 10: Unemployment Rate among Individuals Participating in The Labor Force (15 years and above) In the Occupied Palestinian Territories by Region and Gender, 2008 Quarters and the First 3 Quarters of 2009

Region and Gender	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009
Palestinian Territories (%)							
Male	22.7	26.5	27.3	29.1	25.7	21.6	21.6
Female	21.7	22.7	28.2	22.5	23.8	24.7	24.7
Total	22.6	25.8	27.5	27.9	25.4	22.2	22.2
West Bank							
Male	19.9	16.6	20.5	21.0	20.1	15.1	17.2
Female	15.0	15.2	21.6	14.9	16.8	18.8	20.3
Total	19.0	16.3	20.7	19.8	19.5	15.9	17.8
Gaza Strip							
Male	28.2	45.8	41.2	45.1	36.6	34.9	40.0
Female	39.3	43.3	45.7	42.9	39.0	41.6	54.7
Total	29.8	45.5	41.9	44.8	37.0	36.0	42.3

Source: Palestinian Central Bureau of Statistics, 2009, Labor Force Survey 2008-2009.

The most important characteristics of unemployment in the Occupied Palestinian Territories at present are the following:

- ✧ The highest rate of unemployment is among the youth in the 15-24 age group, especially among females. This means that a large percentage of the unemployed are new entrants to the labor market (see table 11).
- ✧ With regard to years of schooling, there is a major difference between

unemployed males and females. While the rate of unemployment among those having 13 years of schooling or more is higher among females, it was the least among males. This difference has existed for a long time, which indicates that the participation rate grows at a higher rate among females than the growth of demand for females in the labor market (see table 12).

Table 11: Unemployment Rate in the Occupied Palestinian Territory According to Sex & Age Groups, 2008 Quarters and the First 3 Quarters of 2009

Age groups & Sex	Unemployment Rate (%)						
	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009
Both Sexes							
15-24	37.0	39.7	42.1	41.7	39.1	35.7	40.9
25-34	21.9	25.6	27.8	26.7	25.1	23.2	26.9
35-44	16.6	20.5	18.7	22.0	19.5	14.7	16.8
45-54	15.7	18.2	19.7	19.7	17.0	15.1	17.3
55+	11.1	11.9	15.3	19.4	15.6	10.9	10.3
Total	22.6	25.8	27.5	27.9	25.4	22.2	25.8
Males							
15-24	35.0	38.6	39.4	41.7	38.0	33.1	38.7
25-34	21.4	25.4	26.5	27.1	24.0	21.0	23.9
35-44	17.6	22.6	20.7	23.9	21.4	15.6	17.8
45-54	18.2	20.4	22.1	22.5	19.4	17.5	19.7
55+	13.4	14.6	18.2	23.3	17.9	13.1	11.4
Total	22.7	26.5	27.3	29.1	25.7	21.6	24.9
Females							
15-24	47.3	44.6	55.0	41.9	44.6	47.4	51.1
25-34	24.1	26.1	33.1	25.2	29.4	31.0	38.8
35-44	11.2	11.7	9.1	11.8	10.6	10.8	12.4
45-54	3.9	7.8	7.4	5.5	5.2	3.1	5.0
55+	2.9	1.7	2.3	3.0	6.0	0.9	4.6
Total	21.7	22.7	28.2	22.5	23.8	24.7	29.8

Source: Palestinian Central Bureau of Statistics, 2009, Labor Force Survey 2008-2009.

Table 12: Unemployment Rate in the Palestinian Territories by Sex and Years of Schooling, 2008 Quarters and the First 3 Quarters of 2009

Schooling years and Gender	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009
(%)							
Both Sexes							
0	7.8	11.9	16.9	11.9	14.5	13.1	14.8
1-6	23.7	28.9	30.1	33.9	29.2	23.8	27.8
7-9	22.4	27.5	29.1	29.8	27.2	22.0	26.8
10-12	23.8	25.2	25.4	29.5	26.3	22.6	25.1
13+	21.9	24.5	27.9	22.9	22.1	21.8	25.5
Total	22.6	25.8	27.5	27.9	25.4	22.2	25.8
Males							
0	16.0	25.3	27.5	21.6	25.8	23.9	22.7
1-6	26.3	32.9	34.4	38.1	32.8	27.2	31.2
7-9	23.8	29.0	31.1	31.7	28.3	23.4	28.4
10-12	25.4	26.5	26.6	30.6	27.1	23.3	26.0
13+	15.7	19.8	20.2	18.6	17.0	14.7	16.9
Total	22.7	26.5	27.3	29.1	25.7	21.6	24.9
Females							
0	1.2	2.3	4.8	3.1	4.5	0.7	5.3
1-6	8.5	7.5	6.3	7.2	4.9	4.0	6.0
7-9	5.5	11.0	4.4	6.8	11.8	5.5	6.1
10-12	7.3	14.2	12.1	18.1	19.1	15.3	13.1
13+	33.8	33.1	41.8	30.5	31.0	33.7	40.2
Total	21.7	22.7	28.2	22.5	23.8	24.7	29.8

Source: Palestinian Central Bureau of Statistics, 2009, Labor Force Survey 2008-2009.

3.3 Wages and Working Hours

Table 13 illustrates that the average daily wage in the Gaza Strip during the 3rd quarter of 2009 equaled 71% of the average daily wage in the West Bank, and only 42% of the wage of those working in Israel. Those figures were 74% and 44% in the previous quarter. This persisting decline in the average daily wage reflects the circumstances of demand for Palestinian workers under the Israeli imposed siege. It is known that the big gap between the average wage in the West Bank and that in the Gaza Strip is not a new phenomenon. It

existed before the outbreak of the AlAqsa Intifada.

On the other hand, the average daily wage of paid employees in the West Bank registered an increase of 1% only, reaching 87.5 Shekels during the 2nd and 3rd quarters of 2009; while the average wages in the Gaza Strip declined by 3% and rose by 1.2% for those employed in Israel and the settlements between the two quarters (see table 13).

Table 13: Average Weekly Working Hours, Monthly Working Days and Daily Wages in NIS for Paid Workers in the Palestinian Territories according to Place of Work in 2008 Quarters and the First 3 Quarters of 2009

Workplace	(Wages in NIS)			
	Average weekly hours	Average monthly working days	Average Daily wage	Median Wage
Q1 2008				
West Bank	41.2	22.1	84.8	76.9
Gaza Strip	40.2	24.7	63.6	57.7
Israel and settlements	43.0	20.4	139.9	134.6
Total	41.4	22.3	91.5	76.9
Q2 2008				
West Bank	42.7	22.3	86.9	76.9
Gaza Strip	40.0	24.2	61.5	57.7
Israel and settlements	44.3	20.2	143.3	150.0
Total	42.5	22.3	92.8	76.9
Q3 2008				
West Bank	42.8	22.7	82.2	71.2
Gaza Strip	43.4	24.8	57.2	50.0
Israel and settlements	42.5	21.1	138.0	134.6
Total	42.8	22.8	88.9	76.9
Q4 2008				
West Bank	43.1	22.7	87.4	76.9
Gaza Strip	39.9	25.0	61.2	57.7
Israel and settlements	44.7	21.6	138.0	134.6
Total	42.7	23.0	90.6	76.9
2008				
West Bank	42.5	22.4	85.5	76.9
Gaza Strip	40.8	24.7	60.9	57.7
Israel and settlements	43.6	20.9	139.7	146.2
Total	42.4	22.6	91.0	76.9
Q1 2009				
West Bank	42.0	22.1	83.8	76.9
Gaza Strip	38.8	21.3	62.2	57.7
Israel and settlements	42.8	57.7	142.1	150.0
Total	41.5	62.2	89.5	76.9
Q2 2009				
West Bank	42.7	22.6	86.6	76.9
Gaza Strip	39.5	24.9	64.0	57.7
Israel and settlements	42.5	20.1	145.9	150.0
Total	41.9	22.7	76.9	90.7
Q3 2009				
West Bank	43.3	22.7	87.5	76.9
Gaza Strip	41.2	23.9	62.1	57.7
Israel and settlements	41.4	20.2	147.7	150.0
Total	42.5	22.5	93.2	76.9

Source: Palestinian Central Bureau of Statistics, 2009. Labor Force Survey 2008-2009.

3.4 Vacancy Announcements

The number of advertised vacancies during the 3rd quarter of 2009 slightly increased by 1.9% compared to the previous quarter. The total number of vacancy advertisements was

876.³ NGO vacancy advertisements rose by 14.3%; while it dropped in the private and public sectors by 4% and 10.9% respectively. With regard to geographic

³ The number of advertisements that did not specify the number of vacancies were 32.

distribution, the number of advertisements increased in the north, center and south of the West Bank by 1.1%, 2% and 21.9%

respectively; whereas vacancy advertisements decreased in the Gaza Strip by 18.2% (see table 14).

Table 14: Vacancy Announcements in Local Newspapers in the Palestinian Territories (2nd & 3rd Quarters of 2009)

	Q2			Total	Q3			Total
	April	May	June		July	August	September	
Private sector	173	107	242	522	183	144	174	501
Public Sector	5	28	13	46	12	24	5	41
Non-governmental organizations	91	74	127	292	126	127	81	334
Total	269	209	382	860	321	295	260	876
North West Bank	44	14	30	88	27	38	24	89
Central West Bank	195	156	291	642	241	220	194	655
South West Bank	27	23	14	64	30	15	33	78
Gaza Strip	3	16	47	66	23	22	9	54
Total	269	209	382	860	321	295	260	876
Master's degree & above	76	28	40	144	11	17	20	48
BA	153	137	262	552	230	204	198	632
Diploma	40	43	79	162	80	74	42	196
Less than Diploma		1	1	2	0	0	0	0
Total	269	209	382	860	321	295	260	876

Source: Data compiled by MAS from daily local newspapers (Al-Quds, Alayyam and Alhayat).

Table 15 shows the number of vacancy advertisements distributed by sectors and academic qualifications, where the demand for holders of bachelor degrees in the private sector reached 65%, followed by 29% for diploma holders, and 6% for holders of a master degree. In the NGO sector, the demand for holders of a bachelor degree reached 84% and for diploma holders 14%, while it reached 1.8% for holders of a master degree. In the public

sector, the demand for holders of master and bachelor degrees was 29% and 63% respectively.

As for the demand for specializations, it amounted to 39.8% for administration and accountancy, followed by 30.5% for the medical and social sciences specializations, while the demand for specialization in engineering and technology was 29.7%.

Table15: The Number of Advertised Vacancies in Daily Newspapers by Sector and Qualifications during the 3rd Quarter of 2009

	Public Sector	Private Sector	NGOs	Total
Master Degree and above	12	30	6	48
Bachelor Degree	26	326	280	632
Diploma	3	145	48	196
Less than Diploma	0	0	0	0
Total	41	501	334	876

Source: Data compiled by MAS from daily local newspapers (Al-Quds, Alayyam and Alhayat).

BOX 2: Food Security in the Gaza Strip

The subject of food security in the Palestinian Territories has drawn the attention of international organizations. The first assessment of food security in the Palestinian Territories was undertaken in 2003 by three international organizations: the Food and Agriculture Organization – FAO, the World Food Program – WFP and UNRWA. This assessment had been the main point of reference for following developments in food security in the Palestinian Territories.

To begin with, it is worth clarifying the concept of food security as it is recognized internationally. The United Nations Food and Agriculture Organization – FAO and the United States Department of Agriculture – USDA formulated two concepts of food security. According to the FAO, food security is achieved when all people at all times have the physical and economic ability to access sufficient, safe and nutritious food to meet their dietary needs and food tastes, to live an active and healthy life. The concept of food security, from the USDA perspective, is to provide the means for all individuals at all times to access sufficient food for a healthy life.

Underneath both definitions, there are four important elements for food security:

- ✧ The availability of food regardless of the source of this food; whether imported or produced locally.
- ✧ Access to food without physical or economic obstacles.
- ✧ Stability to ensure access to food at all times without fear of emergency shocks.
- ✧ The possibility of healthy food intake (health utilities, safe drinking water and medical care).

The degree of food security is closely linked to the characteristics of households in terms of the size of the household, proportion of women and children in the family, its type of locality, the education level and the employment status of the head of the household. A report was prepared by the FAO and WFP, based on data collected in the Gaza Strip during the 2nd quarter of 2009, entitled ‘A control system for the socio-economic conditions & food security in the West Bank and the Gaza Strip’. It illustrates the relationship between food security with each of the following characteristics:

Family size: unlike families in the West Bank, those in the Gaza Strip are characterized by the lack of variation among them in terms of the absence/presence of food security. This is due to the fact that most of the Gaza Strip households are vulnerable to the same external changes. The average family size in the Gaza Strip amounts to 6.14 individuals. The average family size that enjoys food security is 4.74 individuals versus an average of 6.74 individuals for food unsecured families. This is logical as the per capita income and consumption of food in the larger household is less than in the smaller household.

The proportion of women and children in the family: the basis for the comparison between households in terms of the proportion of women and children is to identify the relationship between food security and dependency rates. The higher the dependency rate on the head of a household increased, the higher the likelihood of vulnerability to food insecurity. In the Gaza Strip there are differences in these proportions, but only slightly, where the women proportion in food unsecured households reached 51% versus 49% in households enjoying food security. The proportion of children in food unsecured households amounted to 49% versus 41% in food secured households.

Type of locality: the type of localities in the Gaza Strip differ from those in the West Bank because of the variations in the demographic structure. In the Gaza Strip, the refugees constitute 68% of the total population whereas this proportion does not exceed 29.8% in the West Bank. Besides that the households in the rural areas of the Gaza Strip, unlike their counterparts in the West Bank, lack ownership of agricultural land holdings. The total area of agricultural lands holdings in the Gaza Strip amounted to 94.6 thousand dunums only, of which 72.5% are owned by the urban population. The total area of agricultural lands holdings in the West Bank amounted to 1781.8 thousand dunums, of which 71.2% are owned by rural families. These disparities expose the rural households in the Gaza Strip, more than other households, to food insecurity. The percentage of food insecurity among these Gazan households reached 67%, which is the worst, followed by families living in the refugee camps, 62%, and the smallest percentage among those living in cities reaching 60%. With regard to food insecurity concentration indicator, it registered the highest percentage of 81% in cities, followed by 16% in the refugee camps and 3% in rural areas. This high percentage in cities is attributed to the fact that cities constitute the largest proportion of the Gazan community.

Education: food security is strongly linked to the level of education for the head of the household. The higher the academic level, the greater the probability of entering the labor market and of earning higher wages than those with less education. This is confirmed by the figures on food security in the Gaza Strip. The heads of households who obtained a bachelor degree or above constitute 46% of the

food secured households as compared to 33% of the households whose heads obtained a secondary certificate or diploma. The remaining 21% are for heads of households who did not reach the secondary education level.

Relation to the labor force: there are two definitions used in the Palestinian Territories for unemployment rates; the first relies on the International Labor Organization - ILO criteria defining the unemployed as those who did not work for an hour during the survey week. The second definition, namely the broad definition of unemployment adopted by the Palestine Central Bureau of Statistics – PCBS, includes in addition to the unemployed as defined by the ILO, the discouraged workers. According to the first definition, the unemployed heads of households in the Gaza Strip until the end of the 2nd quarter of 2009 amounted to 15%, 24% of them lack food security and 2% only are food secured. According to the second definition, the unemployed heads of households formed 24% during the same period, 36% of them lack food security versus 3% only who are food secured. This means that the vulnerability for food insecurity is strongly linked to the head of the households relationship with the labor market, that is to say that the household whose head is unemployed is more vulnerable to food insecurity.

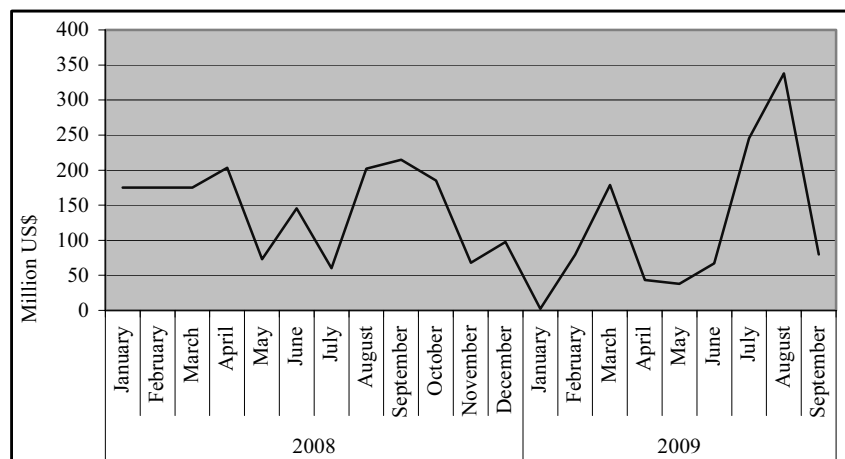
The employment status: the practical status reflects the economic situation for the head of the household. For instance, the living condition of the business owner who employs workers is better than the paid worker whether on regular or irregular pay, and therefore less vulnerable to food insecurity. This logic is confirmed by the food security data. It shows that of the households whose heads are irregular waged workers, 38% lack food security, this is followed by 36% whose heads are regular waged workers, then 21% whose heads are self-employed. The least vulnerable were those households whose heads are business owners constituting 5%.

4. Public Finance Developments

The 3rd quarter of 2009 is characterized by a rise in the public revenues obtained as well as in the corresponding public expenditures. This has been accompanied with a rise in the volume of external aid and assistance extended in support of the Palestinian Authority budget, amounting to \$663 million (a \$515 million difference from the previous quarter) and in contrast to the previous quarters which was characterized by a decline in support, which had put the

Palestinian Authority into a disrupting financial crisis. This rise in the volume of assistance has been achieved mainly by the Saudi Arabian support of \$203 million, the United States support of \$198 million and the European Union support of \$164 million. This support helped the Palestinian Authority to meet its commitments and pay its accrued obligations resulting from the fluctuation and scarcity of revenues during the previous period.

Figure 1: Monthly External Support for the Budget 2008-2009



Source: Ministry of Finance, various reports.

4.1 Financial Performance Developments

4.1.1 Revenues

The 3rd quarter of 2009 witnessed a noticeable positive development on the revenues performance partially connected to the economic activity in the Palestinian Territories, particularly in the West Bank during the first 3 quarters of 2009. The domestic revenues levied by the Palestinian Authority increased in the 3rd quarter of 2009 by 144.5% compared to the previous quarter (the domestic revenues realized in the 3rd quarter of 2009 increase by 13.9% compared to the corresponding quarter of 2008). Domestic revenues amounted to about \$237.9 million, with the tax revenues formulating about \$83 million, 35% of the total domestic revenues. In the meantime, the non-tax revenues constituted 65% at a value of \$154.9 million. It is noticed that the realized domestic revenues up until the 3rd quarter formulated 84% of the amount of \$626 million expected in the 2009 budget, capable of decreasing the 2009 budget deficit in the case that the volume of spending allocated by the budget was not largely surpassed.

The remarkable increase in the domestic revenues for the 3rd quarter is mainly attributed to the increase that occurred on non-tax revenues (a component of domestic revenues) compared to its level in the 2nd quarter. This increase stood at 324% and was because the non-tax domestic revenues fees included an amount of \$100 million as professional fees from the Palestinian Telecommunications Company 'Jawwal' for merging with 'Zein' company. \$60 million came from 'Jawwal' and \$40 million from 'Zein', received in July 2009.⁴ Whilst the other components of non-tax revenues continued to range within their quarterly levels and amounted to about \$154.9 million. The increase in the domestic revenues was enhanced with an increase in tax revenues (the other component of domestic revenues) by 37%. Here the realized tax revenues increased by \$22.2

million, reaching \$83 million as a result of the improvement that occurred on the collection of income tax as well as the remarkable improvement in the value added tax VAT, as the amount levied in the 3rd quarter increased by \$15.2 million more than the 2nd quarter. This was in view of the constant efforts to control the evasive attempts of merchants to pay this tax. An increase of \$4.6 million is also noticed on the cigarettes excise (one of the tax revenues components) as a result of the raising of these excises by the Customs Department at the Ministry of Finance, which was increased more than once during 2009.

As for the clearance revenues,⁵ obtained as a result of commercial dealings between the Palestinian Authority and Israel, the amount transferred to the Ministry of Finance during the second quarter totaled \$312 million, with an increase of 20% from the amount transferred in the 2nd quarter. The clearance revenues transferred in the 3rd quarter constituted 27.8% of the revenues expected in the 2009 budget amounting to \$1,123 million.

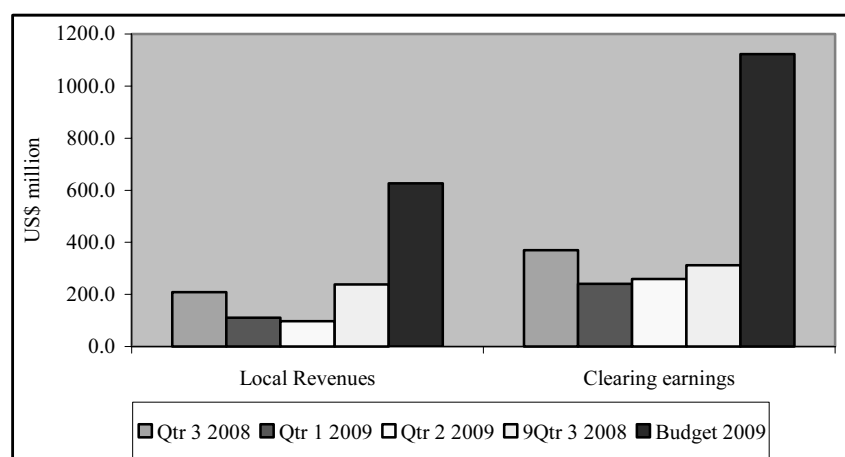
With the developments that took place in domestic revenues and clearance revenues, the total amount of revenues during the 3rd quarter was about \$549.9 million; while the tax returns⁶ amounted to around \$99 million, recording a considerable increase as compared to previous quarters due to the transfer of the accumulative fuel tax returns to the General Petroleum Corporation in July 2009. The total net revenues reached \$450.9 million, with a rise of 26.8% compared to the 2nd quarter and a decline of 18.7% of the level realized in the 3rd quarter of 2008. The realized net revenues in the 3rd quarter of 2009 accounted for 27.6% of the amount expected to be collected this year, i.e. \$1,631 million, which means that an additional \$43.2 million was recorded as current surplus in 2009.

⁴ It is known that the merge bargain between the two companies did not work out. This was because the period of time agreed upon to finalize the bargain expired before meeting the requirements and main conditions for concluding the agreement in accordance with the resolutions issued by the Palestinian Telecommunication Co. board meeting, held on the 19th of November 2009.

⁵ The clearance revenues declined in the 1st quarter by 16.8% and 1.3% compared to the first and 4th quarters of 2008 respectively.

⁶ Tax returns comprise the value added tax VAT returns, the returns on oil products, the returns for tax-exempted organizations. The 2009 budget expects that returns would amount to \$118 million during this year.

Figure 2: Public Revenues Developments in the 3rd Quarter of 2009



Source: Ministry of Finance, Financial Transactions Report, Revenues, Expenditures and Sources of funding, September 2009.

4.1.2 External Financing

The external financing in support of the Palestinian Authority budget continued to be a source of worry for the public finances during the previous quarters in view of the state of fluctuations and instability in this regard. Since the 4th quarter of 2008, the assistance received started to decline until the volume of assistance reached its lowest levels during the 2nd quarter of 2009 because of the abstention of the donor countries and their delay in transferring the amounts pledged to the Palestinian authority. This was in light of the political developments that had taken place and are still ongoing in the Palestinian arena on the one hand, and due to the repercussions of the international financial crisis that hit these countries on the other hand. As a result of this, the Ministry

of Finance got into a real crisis which limited its capacity to meet its financial obligations in due time, forcing it to resort to borrowing from commercial banks in order to provide the liquidity needed for the requirements of urgent expenditures while delaying others. The matter that had pushed the Palestinian Authority to urge the donor countries to fulfill their commitments and salvage the Authority from the crisis it was undergoing. However, the 3rd quarter was different than the preceding quarters when the value of grants received by the Palestinian Authority had significantly risen by 347.3%, reaching record levels as compared to the previous quarter and by 39% as compared to the 3rd quarter of 2008 (see table 16).

Table 16: Public Revenues Development in the 3rd Quarter of 2008 - the 3rd Quarter of 2009, Compared with 2009 Budget

Item	(USD million)						Percentage Change in Q3 Vs. Q2 (%)	Share of Q3 of 2009 in the Budget (%)
	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009	2009 budget		
Total Net Revenues *	554.8	302.9	334.9	355.7	450.9	1631	26.8	27.6
Tax Returns	24.1	11.5	17.3	0.7	99.0	118.0	14042.9	83.9
Total Revenues	578.9	314.4	352.2	356.4	549.9	1749	54.3	31.4
Domestic Revenues	208.9	121.6	111.1	97.3	237.9	626	144.5	38.0
Tax Revenues	62.8	61	71.2	60.8	83.0	273	37	30.4
Non-tax Revenues	146.1	60.6	39.9	36.5	154.9	353	324	43.9
Clearance Revenues	370	192.8	241.1	259.1	312.0	1123	20	27.8
Grants and Assistance	476.1	351	278.3	161.0	668.4	1653	315.2	40.4
Grants in Support of Budget	476.1	351.1	259.2	148.3	663.3	1150	347.3	57.7
Grants in Support of Development projects	NA	NA	19.1	12.7	5.1	503	-59.8	1
Total Public Revenues and Grants	1055	666	630.5	517.4	1218.3	3402	135.5	35.8

Source: Ministry of Finance, Fiscal Operations Report, Revenues, Expenditure and Funding Sources, September 2009.

* The Total net revenues are the total of revenues after the deduction of tax returns.

The total amount of grants and assistance provided in support of the budget during the 3rd quarter was around \$662.6 million. Grants provided by Arab states amounted to \$217.8 million constituting 33% of the total amount of grants and assistance. Egypt and Saudi Arabia contributed \$15 and \$202.8 million respectively. It is noted that the

provided Arab support which had declined in the last quarters, especially since the beginning of the 4th quarter of 2008, started to rise in this quarter by 932% compared to the 2nd quarter of the 2009 and by 38% compared to the 3rd quarter of 2008 (see table 17).

Table 17: Structure of External Assistance to the Palestinian Authority in the 3rd Quarter of 2008 - the 3rd Quarter of 2009

Donor	Q3					Percentage of total budget support grants in 3rd quarter of 2009
	2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009	
Arab Grants	158	56	73.9	21.1	217.8	32.9
Arab League	0	0	0	0	0	0
Algeria	0	0	26	0	0	0
Egypt	14.6	0	0	3	15	2.3
Saudi Arabia	100.7	56	22.9	15.4	202.8	30.6
Oman	0.0	0.0	0.0	2.9	0.0	0
United Arab Emirates	42.7	0	25	0	0	0
International Grants	318.1	295	185.3	128.0	444.8	67.1
PEGASE mechanism*	181.6	115.1	94.2	120.3	164.0	24.8
European Union	0	0	0	0	0	0.0
India	0	0	10.1	0	0	0.0
China	0	0	0	0	0	0.0
France	0	0	27.7	0	0	0.0
Japan	0	9.5	0	0	0	0.0
Russia	9.9	0	0	0	0	0.0
The United States of America	0	150	0	0	98.51	30.0
Greece	0	0	0	3	0	0.0
Turkey	0	0	0	0	10.2	1.6
World Bank (or through the Bank)	118.9	16.2	50.6	0.0	28.8	4.3
Grants for the Palestine Central Bureau of Statistics (PCBS)	0	0	0	0	0	0.0
Services Support Emergency Program **	7.7	4.2	2.7	3.9	3.9	0.5
Grants for the Ministry of Social Affairs	0	0	0	1.1	0	0.0
Development Grants	0	0	0	0	40.2	6.1
Total Budget Support	476.1	351	259.2	149	663.5	100
Development Projects Support Grants***	0	0	19.1	12.7	5.1	—
Total External Grants & Assistance	476.1	351	278.3	161.8	667.7	—

Source: Palestinian Ministry of Finance, Fiscal Operations Report, Revenues, Expenditure and Funding Sources, September 2009.

* The Palestinian European Mechanism for Social & Economic Assistance (PEGAS), was launched on Feb 1, 2008 for the provision of financial support from the EU and other international parties to the PNA for 3 years in alignment with the Palestinian Reform and Development Plan (PRDP). Thus, all EU assistance to the Palestinians was channeled through this mechanism following the 1st Quarter of 2008.

** In support of health, education, water and electricity services.

*** Refers to the donors direct grants allocated for the implementation of development projects that are not included in the budget. No quarterly data is available on those grants. However, 2008 data indicates that the total grants for 2008 reached \$250 million, but it is believed that it did not actually exceed \$190 million.

On the other hand, international grants constituted 67.7% of the total amount of

grants and assistance provided at the value of \$444.8 million, with a rise of about 40%

compared to 2nd quarter and by 405% more than what was provided in the 3rd quarter of 2008. Unlike the usual case, the United States was the prime international donor in this quarter, excelling over the European Countries that are considered the largest international donors for the Palestinian Authority. The United States transferred \$198.5 million, delivered in June in shekels, at the value of NIS 772 million. As for the European countries that provide assistance through the Palestinian European Mechanism for Social & Economic Assistance (PEGAS), they transferred a total of around \$164 million during this quarter. This was followed by World Bank grants, whether provided by various countries through the World Bank or those provided as development grants, or within the emergency services support program, which amounted to a total of \$72.9 million. It is noted that the total grants provided in the 3rd quarter of 2009 in support of the budget comprised more than half the total grants in support of the budget as expected in the 2009 budget (about 57.7%). This was a clear indication of the interest of donor countries in the financial situation of the Palestinian authority following the crisis of the first months of the year.

With regard to the grants in support of the community development projects, provided by the donor countries in assistance for development projects targeting the implementation of infrastructure projects, they amounted to \$5.1 million in the 3rd quarter of 2009. The support provided for development projects in this quarter constituted only 1% of the amount expected in the budget, while the total grants provided since the beginning of the year until the 3rd quarter was about \$37 million, i.e. 7.3% of the amount of \$503 million, expected in the 2009 budget. This indicates that the pattern of development grants is no different that of previous years, where the actually disbursed amount falls short by half of what was actually projected in the budget.

4.1.3 Expenditures

The remarkable increase in the total public revenues and grants in the 3rd quarter of 2009 was accompanied with a significant increase in the total expenditures and net lending as well as a 53.4% increase

compared to the 2nd quarter. This following a decline of 9.7% over the corresponding period of 2008, due to the cash payments of arrears accumulated in the government in the year 2008. These expenditures amounted to \$960.7 million, equivalent to 34.6% of the amount projected in the 2009 budget (i.e. the unexpected budget deficit increased by \$265.7 million), which is a considerable amount in view of the high expenses in this quarter.

The wages and salaries bill, which includes civilian and military personnel salaries and wages, amounted to \$511.3 million in the 3rd quarter of 2009, with a rise exceeding 56% compared to the 2nd quarter of the same year (and a drop of 11.1% from the 3rd quarter of 2008). This rise is attributed to two batches of payments, the October bill (\$148.5 million), which had been paid in advance in September, in addition to the September bill (\$131.4 million) in order to assist the public sector employees in meeting the exceptional requirements of feast period.⁷ In addition, the Ministry of Finance paid \$23 million in compensation for employees who obtained loans from commercial banks operating in the Palestinian Territories in the year 2006.⁸

The non-wages expenditures (operational, transfer payments and capital expenditures) increased in the 3rd quarter of 2009 by 90.3% compared to the second quarter, and by 2.9% compared to the 3rd quarter of 2008, reaching \$360.3 million. This substantial increase is attributed to the government payment of dues that accumulated during the 1st and 2nd quarters for the private sector. This was in addition to the payment of the operational arrears for bills that were due in the year 2008 at the

⁷ The government usually pays the bill of wages and salaries in advance when the end of month and the feast season coincide, in an attempt to assist employees and their families in meeting the special requirements of the feast period. This has been done in 2008 as well.

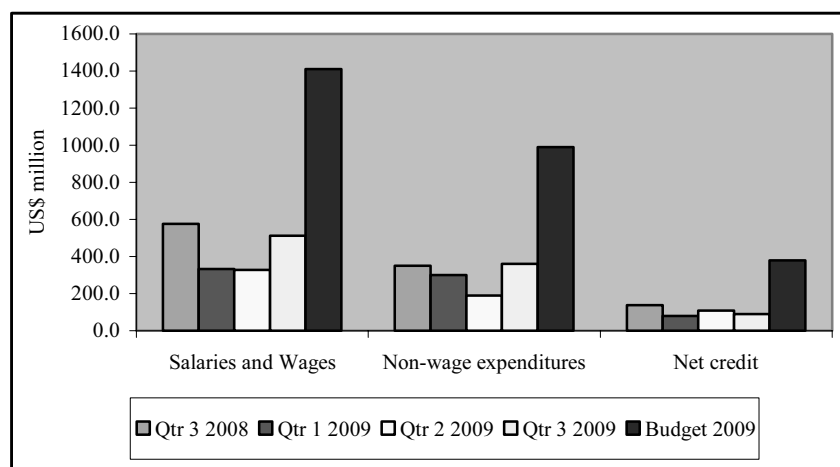
⁸ During the financial crisis experienced by the Palestinian Authority in 2006 and its inability to pay the salaries of its employees, who could not pay back their loans from commercial banks at that time. Subsequently, a tripartite agreement has been concluded (between the government, the banks and the workers union) stipulating, with the consent of the workers union on behalf of the employees, to pay back all their loans to the banks, after fixing the interest rate and the compensation by the government. According to this commitment, the government was required to pay \$23 million in compensation in October 2009, but this pledge had been fulfilled on the 17th of September 2009.

value of \$133 million.⁹ The government also had increased the allocations for the families of the martyrs and wounded during the 3rd quarter on top of their ordinary monthly allocations.

It is worth mentioning that this item rose up by \$300 million in the 2009 budget (from \$990million to \$1290 million) after the endorsement of the Palestinian Ministerial cabinet on the supplement of the budget law by the end of September 2009,¹⁰ by allocating

\$200 million for transfer payments expenditures and \$100 million for operational expenditures, to be spend in the Gaza Strip to improve the infrastructure there. This had obliged the government to request additional appropriations to cover these expenses from donor countries.¹¹ The wage & non-wage expenditures and net lending comprised about 53%, 38% and 9% of the current expenditures respectively in the 3rd quarter of 2009 (see figure 3).

Figure 3: Public Expenditures Developments in the 3rd Quarter of 2009



Source: Palestinian Ministry of Finance, Fiscal Operations Report, Revenues, Expenditure and Funding Sources, September 2009.

With regard to the item of net lending, it has been an area of great concern for the government whose purpose it is to reduce and limit its growth as it constitutes a burden on public expenditures. The Government continued with its measures of reform for the local authorities through sustaining the policies adopted by the government in the 2009 budget and derived from the Palestinian Reform and Development Plan (PRDP) to ensure financial sustainability. Net lending amounted to \$98.1 million in the 3rd quarter. This constituted a 18.5% decline from the 2nd quarter of 2009 and was 35.6% lower than the 3rd quarter of 2008 (an indication of the improvement of the

collection of electricity bills by the local councils and municipalities), constituting about 23.4% of the amount targeted in the 2009 budget. The budget projected the spending of \$380 million only during the current year which is \$67 million less than what was spent during 2008. This is in line with the government policies regarding the reduction of net lending.

The development expenditures which targets the implementation of community development projects that are partially financed through direct funding from donors amounted to \$65.9 million, with an increase of 37.6% compared to the 2nd.

⁹ It is worth noting that these expenses were not included in the 2009 budget at the time when it was prepared but have suddenly appeared after the Ministry of Finance received bills from various ministries, that were due in 2008 and unpaid, thus had to pay for them.

¹⁰ After the request of \$300 million by the Ministry of Finance to spend in the Gaza Strip, the Palestinian Ministerial Council approved the request of additional allocations within the non-wages expenditures (operational and transfer payments) on the 29th of September, 2009. This was included in the 2009 budget, the matter that will raise the projected current deficit from \$1.15 billion to \$1.45 billion.

¹¹ This increase may seem to correspond to the governments efforts to raise the proportion of non-wages expenditures from total current expenditure in order to increase the efficiency of services provided by the ministries and public institutions. Nevertheless, this increase was allocated to cover other exceptional expenses in the Gaza Strip.

quarter It is noted that external assistance delivered directly for the implementation of these projects amounted to \$5.1 million (7.7% of the development expenditures in the 3rd quarter). The proportion of development expenditures during the 3rd quarter accounted for 13.1% of the targeted

amount in the 2009 budget. The rate of what had been spent since the beginning of the year reached 25% only, which is lower by \$378 million than the amount planned for spending on development projects within the budget of 2009 (see table 18).

Table 18: Development of Public Expenditures for the 3rd Quarter of 2008 – the 3rd Quarter of 2009, Compared with the 2009 Budget

	(USD million)							
	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009	Budget 2009	The change in Q3 Vs. Q2 2009 (%)	Proportion of Q3 2009 in the Budget(%)
Wages and salaries	575.4	262.2	333.3	327.6	511.3	1410	56.1	36.3
Non-wage expenditures	350.1	248.1	300.6	189.3	360.3	1290	90.3	36.4
Net Lending	138.4	107.7	78.5	109.3	89.1	380	-18.5	23.4
Total expenditures and net Lending	1064	618	712.4	626.2	960.7	2780	53.4	34.6
Development expenditure	NA	NA	11.1	47.9	65.9	503	37.6	13.1

Source: Palestinian Ministry of Finance, Fiscal Operations Report, Revenues, Expenditure and Funding Sources, September 2009.

4.1.4 Surplus (Deficit)

In view of the developments in the financial performance, witnessed during the 3rd quarter of 2009, in revenues and expenditures and with the significant rise in domestic net revenues 94,450.9 million), in addition to the rise in total expenditures and net lending (\$960.7 million), the current budget deficit amounted to \$509.8 million. With the addition of external support of the budget (\$663.3 million), the current deficit is reduced to a surplus of \$153.5 million. Total budget deficit (current deficit in addition to development expenditures) prior to external budget support, amounted to

\$575.7 million. With the external support and an amount of \$5.1 million in support of community development projects (development expenditures), total budget deficit amounted to about \$92.7 million (see table 19). During the 3rd quarter of 2009, an amount of \$345 million was paid in July and August as part of the loans for commercial banks. The government had borrowed \$211 million to pay the wages for September and October together in September, leaving the net payment for banks at about \$133 million during the 3rd quarter of 2009.

**Table 19: Budget Surplus (Deficit) Developments
For the 3rd Quarter of 2008 – the 3rd Quarter of 2009, and the 2009 Budget**

	(USD million)					
	Q3/ 2008	Q4/ 2008	Q1/ 2009	Q2/ 2009	Q3/ 2009	2009 Budget
Current Budget Surplus (Deficit)	(509.1)	(315.1)	(377.5)	(270.5)	(509.8)	(1150)
Current Budget Surplus (Deficit) After External Support of the Budget	(33)	36	(118.3)	(122.2)	153.5	0
Total Budget Surplus/Deficit (Including Development Expenditures) Prior to External Support of the Budget	NA	NA	(388.6)	(318.5)	(575.7)	(1653)
Total Budget Surplus/Deficit (Including Development Expenditures) After External Support of the Budget and Support of Development Expenditures	NA	NA	(110.3)	(157.5)	92.7	0

Source: Palestinian Ministry of Finance, Fiscal Operations Report, Revenues, Expenditure and Funding Sources, September 2009.

Figures in brackets are negative.

The Government continues to work according to directions and policies adopted in the midterm Palestinian Reform and Development Plan (PRDP) that the government started to implement at the beginning of 2008. The budget of 2009, implemented by the government, comprises policies that supplement the PRDP vision which mainly aims to achieve sustainable financial stability.

Regarding the policy pursued by the government for the reduction of recruitment and allowances in order to limit the growth of the wages bill, the number of employees (civilians and military) reached about 147,153 employees by September 2009. This figure is less than the 153 thousand allocated for the year 2009, in light of the agreement between the Palestinian

Authority and donor countries to improve and develop government performance. The number of civilian employees increased by 520 employees during the 3rd quarter, while the number of military staff increased by 906. It is worth mentioning that civil servants increased during the first 3 quarters of 2009 by about 1,965 employees (in the education, health and social sectors). An increase of 2,231 military personnel was also witnessed (to increase the security services personnel, especially after the redeployment of the Palestinian security forces and police in some areas under the control of the Palestinian Authority, within the governments plans, which aim to maintain order and security). The total number is 4,216, both civilians and military staff.

BOX 3: The Issue of Electricity in the Palestinian Territories

The electricity sector suffers from numerous difficulties that have been accumulating for decades. The Palestinian Territories lack local sources of energy and thus depend on imports to meet the needs of the Palestinians for electricity. The value of electricity imports has constituted about 8% of the Palestinian total commodity imports in recent years. There is an almost exclusive reliance on the Israelis to provide the Palestinian areas with its required electricity. This, with the exception of the small amount (30-90 megawatts) produced by the Palestinian Electricity Company in the Gaza Strip, which does not constitute, at best, more than 6% of the Palestinians total need for electricity. During 2008, the Jericho and Rafah municipalities were provided with electric power through interconnection projects with Jordan and Egypt. In spite of the relatively low contribution¹² of these projects in covering the Palestinian need for electricity, it was an important step in the right direction to phase out and reduce the dependency on Israel with regard to the supply of electricity.

The situation of the electricity sector in the Gaza Strip is considered one of the problems disturbing decision makers in the Palestinian Authority and citizens alike. The supply of electricity for the Gaza strip comes from 3 sources: the Israeli side, that provides about 52% of the required electricity, the Egyptian side, that provides about 8%, and the Palestinian Electricity Company that provides 40% when it operates at full capacity. The company obtains the necessary fuel for power generation from the Israeli side.

A number of factors contribute to the electricity crisis in the Gaza Strip, as the supply of electricity from Israel is affected by political and security developments. Hence, Israel utilizes the electricity issue as a political tool against the Palestinians. On the other hand, the provision of finances necessary for the purchase of fuel used to run the generators of the Palestinian Electricity Company is considered one of the reasons for the crisis that affects the electricity sector in the Gaza Strip. The European Union pledged to finance the purchase of the amount of fuel needed by the station but had stopped the funding, following the political events in the Gaza Strip, by mid 2007. The EU resumed its funding for the station later, then stopped completely again in November 2009 when the Palestinian Authority in Ramallah started to pay the prices necessary to operate the power station at an amount reaching NIS 37 million a month. The persisting crisis in the electricity sector in the Gaza Strip is attributed to the deteriorating economic conditions, due to the siege, poverty, the weak performance of the local authorities and the electricity distribution company in its poor collection of electricity bills from citizens in the Gaza governorates. This has resulted in the inability of the company to cover operating and power generation expenses and has also burdened the public treasury as it spends hundreds of millions annually to pay electricity bills on behalf of citizens.

¹² Palestinian imports of electrical power from Jordan amounted to \$6.4 million and to \$9.9 million from Egypt during the year 2008.

In conclusion, the electricity sector in the Palestinian Territories requires studying and serious review in order to organize and coordinate efforts, by various international, regional and local parties, to find fundamental and viable solutions in response to the challenges facing this vital sector. Also to mobilize financial, technical and human support for the development of this sector and for the provision of the Palestinian needs of electricity supply at a reasonable price and of adequate quality.

5. Banking Developments

The consolidated balance sheet of banks operating in the Palestinian Territories at the end of the 3rd quarter of 2009 indicated a continuation of the positive growth in most of the banking indicators, compared to the previous quarter of the year. It points to:

- ❖ Total growth in bank assets by more than 5%.
- ❖ Increase in client deposits by more than 6.6%.
- ❖ Increase in paid capital of banks by nearly 1.6%.
- ❖ Growth of net credit facilities' portfolio by 7.7%.
- ❖ Increase in balances with banks abroad by more than 7%.
- ❖ Increase in the balances of banks with the Palestine Monetary Authority (PMA) by nearly 4.7%.

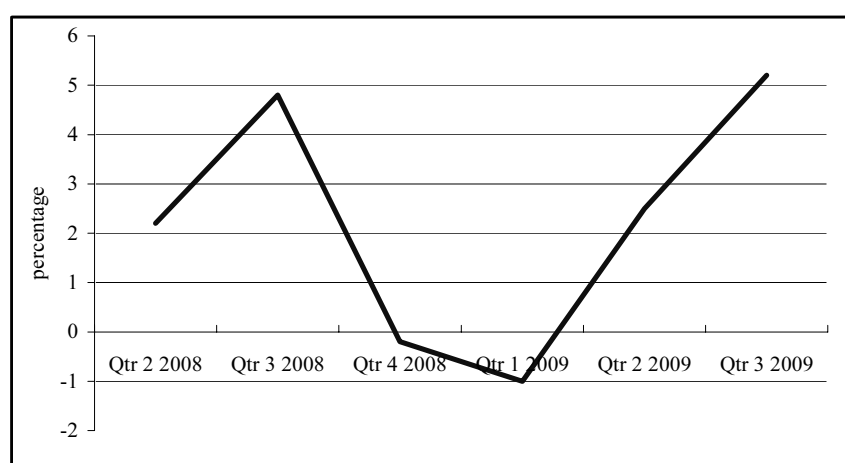
- ❖ Increase in checks presented for clearance by 9.8% besides an increase in the number of bounced checks by nearly 1%.

5.1 Banks' Consolidated Balance Sheet

5.1.1 Assets

Data of the consolidated balance sheet of banks operating in the Palestinian territories indicates that banks' total assets exceeded \$3 billion by the end of the 3rd quarter of 2009. That means an increase of 5.2% for these assets as compared with the previous quarter and by 6.5% compared to the corresponding period of the year 2008 (see figure 4).

Figure 4: Growth Rate Development on Assets of Banks Operating in the Palestinian territories (2nd Quarter 2008 – 3rd Quarter 2009)



Source: The Palestine Monetary Authority (PMA)

Looking at the structure of bank assets, we notice that bank investments abroad increased by the end of the 3rd quarter of 2009 by 7.1%, compared to the 2nd quarter

of the same year; with a decline by about 13% compared to the corresponding period of last year. This is a result of PMA instructions calling on banks to reduce their

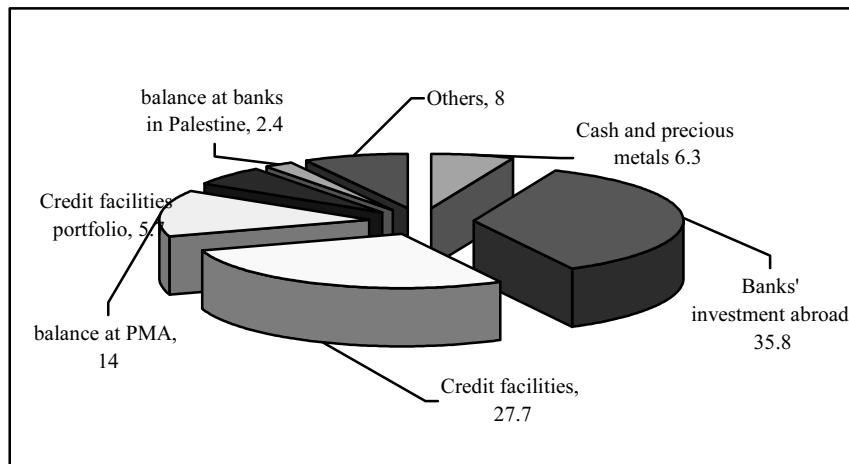
investments abroad, not to exceed 55% of total deposits by the end of August 2009. Obviously, the PMA purpose is to stimulate banks to increase local credit facilities to encourage investment in the Palestinian economy.

In spite of the rise in banks' investments abroad by the end of the 3rd quarter of 2009, it remained below the maximum limit allowed by the PMA as it did not exceed 46%. As a result, direct credit facilities increased by 7.7% during the 3rd quarter of 2009 compared to the previous quarter and by 25% compared to the corresponding quarter of the year before. The reduction of

the proportion of investment abroad to total deposits (in line with the PMA instructions) had led to a rise in the proportion of credit facilities to total deposits. This went from 35.1% in the 2nd quarter to 35.4% in the 3rd quarter of 2009 when total credit facilities amounted to \$2,261 million, comprising of 64% loans and 31.5% overdraft (see figure 6).

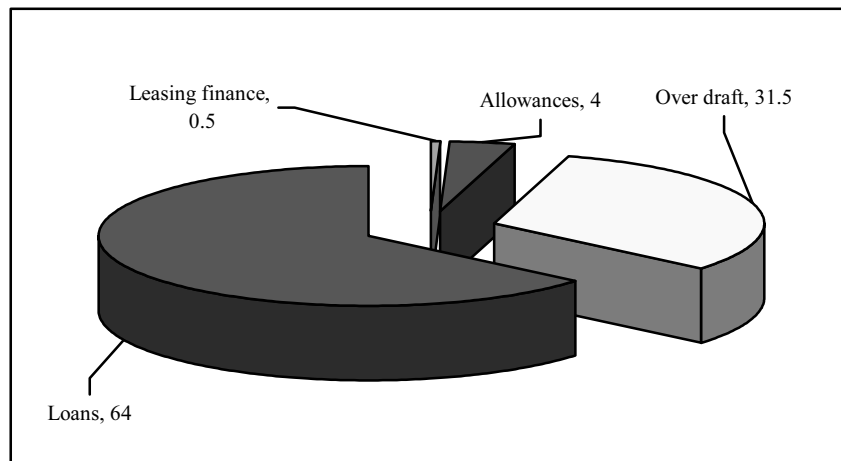
On the other hand, banks' balances with PMA have risen at the end of the 3rd quarter of 2009 by about 5% compared with the previous quarter and by nearly 8% compared with the 3rd quarter of 2008 (see figure 5).

Figure 5: The Structure of Assets of Banks Operating in the Palestinian Territories (End of 3rd Quarter 2009)



Source: PMA - The consolidated budget of banks.
Others include: banks acceptances, investments, fixed assets and other assets.

Figure 6: Distribution of Credit Facilities by Type (End of 3rd Quarter 2009)

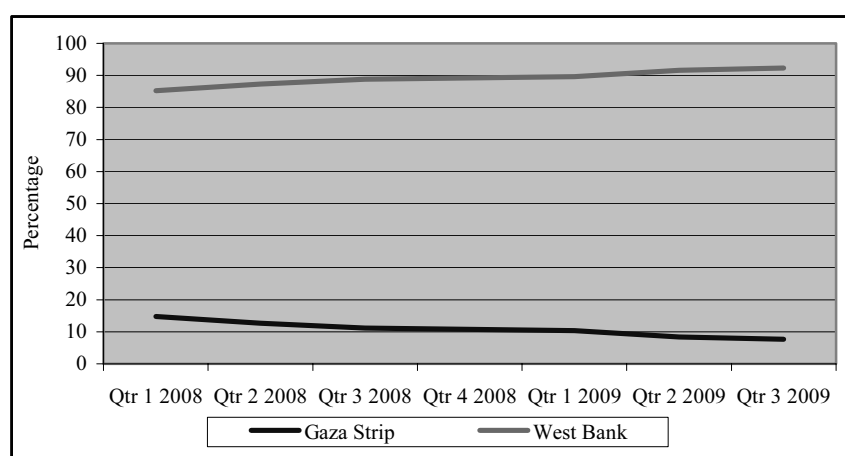


Source: PMA - The consolidated budget of banks.

The credit facilities were divided between the private and public sectors by 68% and 32% respectively. Thus, by the end of the 3rd quarter of 2009, the credit facilities extended to the public sector had declined in favor of the private sector by about 4% from the level achieved by the end of the previous quarter. In contrast to the above positive distribution of credit facilities, the distribution by geographic region (the West Bank and the Gaza Strip) reflects a negative image. This is represented in the continuous

decline in credit facilities in the Gaza Strip, whether in value or in the proportion to total facilities. Credit facilities extended in the Gaza Strip comprised 7.7% of the total facilities by the end of the 3rd quarter of 2009, compared to 8.4% in the previous quarter and 11.2% in the corresponding quarter of last year (see figure 7). This decline in the Gaza Strip is a manifestation of the economic reality that has been undergoing an increasing deflation for several years at all levels.

Figure 7: Distribution of Credit Facilities by the West Bank and the Gaza Strip (1st Quarter 2008 – 3rd Quarter 2009)



Source: PMA - The consolidated budget of banks.

The credit facilities extended were also distributed by various trading currencies in the West Bank and the Gaza Strip during the 3rd quarter of 2009, at varying rates where the USD remained dominant at 61.4% versus 28.8% for the NIS, 9.2% for the JoD and 0.6% for other currencies. When compared with previous periods, a continuous decline is noticed in the proportion of credit facilities extended in the USD in favor of the NIS. When compared with the 3rd quarter of last year, the USD share has declined by 2% while the NIS share has risen by a comparable amount. It appears that the instability of the USD exchange rate on one hand and the high exchange rate of the NIS on the other has pushed towards the persistence of this

change in the shares of both currencies of credit facilities (see table 20).

The cash and precious metals items has risen by 3% in the 3rd quarter, compared to the previous quarter, and by over 88% as compared with the corresponding quarter of the previous year. The portfolio investment for trading and investments has also risen by 8% by the end of the 3rd quarter, in comparison with the 2nd quarter and by more than 120% in comparison with the corresponding quarter of the previous year. Other items have also risen including fixed assets by 0.7% and other assets by 6.6% by the end of 3rd quarter compared to the 2nd quarter.

**Table 20: The Distribution of the Direct Credit Facility Portfolio
(1st Quarter 2008 – 3rd Quarter 2009)**

Budget Item	(USD Million)						
	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009
By Geographical Distribution							
West Bank	1460.7	1509.1	1603.1	1625.5	1650.7	1924.2	2087.3
Gaza Strip	313.2	237.6	204.4	202.7	192.2	175.5	173.6
By Depositing Party							
Public Sector	511.3	511.3	544.8	532.7	581.6	748.8	722.2
Private sector/resident	1191.3	1140.5	1129.6	1165.9	1123.2	1216.2	1365.2
Private Sector/non-resident	82.0	95.3	133.1	129.6	138.1	134.7	151.0
By Type of facility							
Loans	1062.0	1066.5	1109.2	1114.2	1159.0	1338.9	1500.2
Overdrafts	700.9	669.3	687.8	703.7	673.6	750.7	753.3
Leases	10.9	10.8	10.5	10.3	10.3	10.2	7.5
By Type of Currency							
US Dollar	1159.5	1117.7	1163.1	1190.2	1225.9	1301.7	1388.6
Jordanian Dinar	173.5	151.1	146.2	147.5	142.5	200.3	208.5
New Israeli Shekel	419.4	463.1	483.9	474.3	460.6	582.7	650.7
Other	21.4	14.7	14.3	16.2	13.8	15.0	13.1

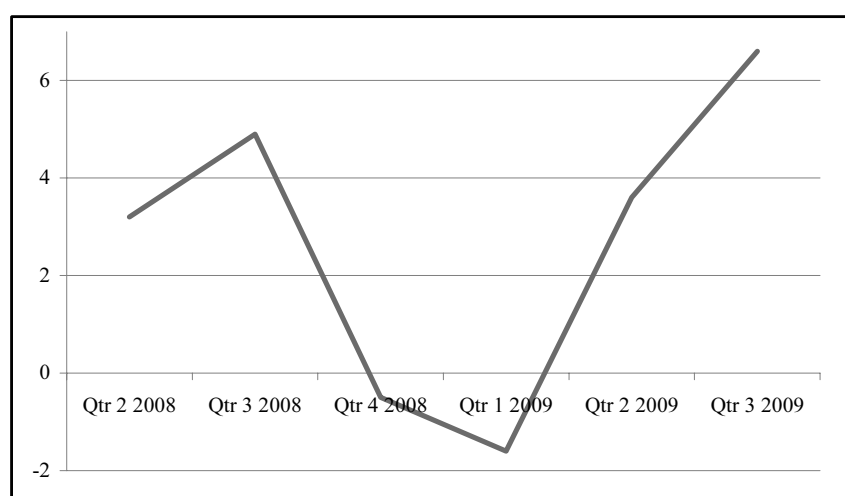
Source: PMA - The consolidated budget of banks.

5.1.2 Liabilities

The clients' deposits are the main component of the total liabilities of banks operating in the Palestinian territories, constituting 78.3% of the total liabilities by the end of the 3rd quarter of 2009. The continuing rise in this item year after year is considered an inherent characteristic in spite

of the seasonal disparities that appear on the quarterly or monthly levels. Client deposits increased by 6.6% by the end of the 3rd quarter compared to the previous quarter, and by over 8.7% compared to the corresponding quarter of the previous year.

**Figure 8: Clients' Deposits Development
(1st Quarter 2008 – 3rd Quarter 2009)**



Source: PMA.

The clients' deposits were distributed into the private and the public sectors' deposits by 90% and 10% respectively. Comparing

these figures with the previous quarter of 2009 shows a decline in the contribution of the private sector deposits by about 1.5% in

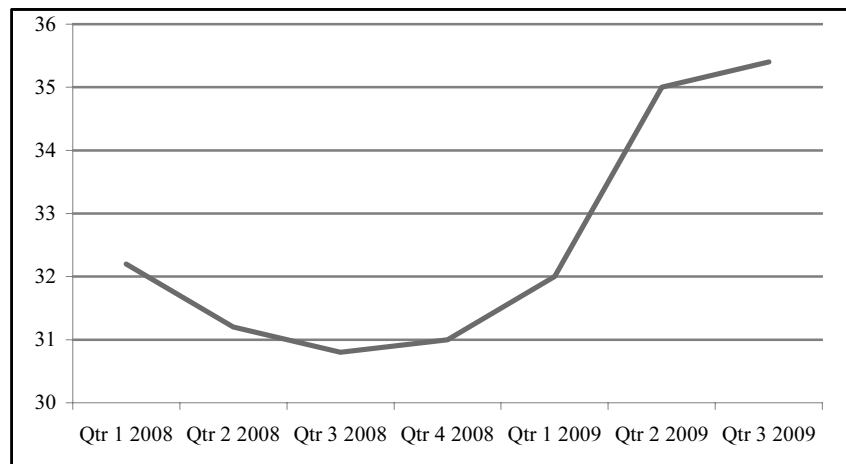
favor of the public sector deposits. Nevertheless, these figures did not change in comparison to the corresponding period of last year. When clients' deposits are distributed by type, 39.6% of those deposits are current account and demand deposits, 24.7% are saving account deposits and 35.7% are time deposits.

The West Bank contributes to around 84.7% of total clients' deposits, whereas the Gaza Strip contribution is 15.3%. There is also a disparity in the distribution of clients' deposits by type of currency, as the USD dominated with over 43.1% of total

deposits. The share of the JOD and the NIS amounted to 27.3% and 23.8% respectively and 5.8% for other currencies.

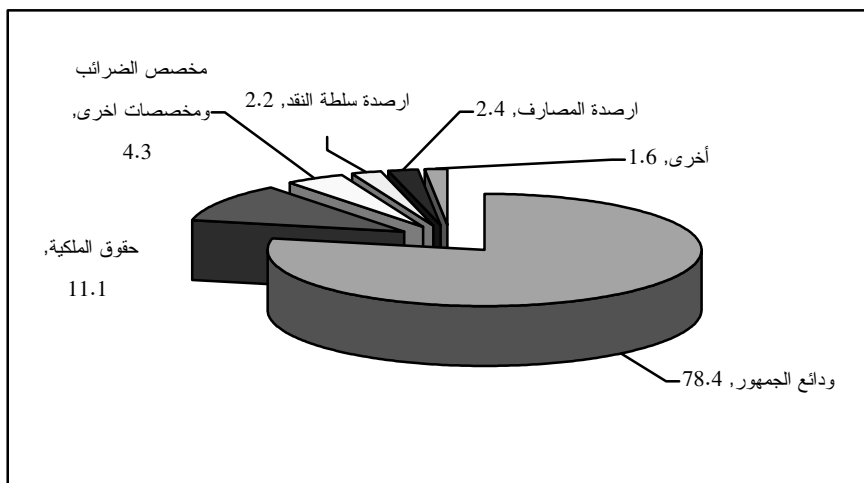
A continued improvement is noted in the proportion of credit facilities to total deposits. It had risen by 35.4% by the end of the 3rd quarter of 2009, compared to 34% in the previous quarter, while it was below 31% by the end of the corresponding quarter of last year (see figure 9). In spite of the constant rise in this proportion, it remains below the prevalent levels in neighboring countries.

Figure 9: Credit Facilities Ratio to Total Client Deposits (1st Quarter 2008 – 3rd Quarter 2009)



Source: PMA.

Figure 10: The Structure of Liabilities in Banks Operating in the Palestinian Territories By the End of the 3rd Quarter 2009



Source: PMA.

Others include: other liabilities, acceptances executed and outstanding and banks' balances abroad.

Equity has risen by 3.6% at the end of the 3rd quarter of 2009 compared to the previous quarter and by 11.6% above its level in the corresponding quarter of last year. The paid up capital, which is the main component of equity, increased by 1.6% in the 3rd quarter of 2009 in comparison with the previous quarter and by 18% compared to the

corresponding quarter of last year. The PMA balances with banks increased by 24%, while banks' balances with other banks in Palestine declined by 23% in the 3rd quarter of 2009. Provisions for tax and other provisions increased by about 2.7% compared to the previous quarter (see figure 10).

Table 21: Banks' Consolidated Balance Sheet (1st Quarter 2008 – 3rd Quarter 2009)

Budget Item	(USD Million)						
	2008				2009		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Cash & Precious Metals	357.3	367.5	273.9	346.2	334.6	501.0	515.8
Balances with the PMA & Banks	4492.9	4332.2	4708.9	4674.0	4513.5	4086.8	4265.3
Investments Portfolio	185.7	217.9	214.4	206.6	233.1	429.7	467.5
Direct Credit Facilities	1773.1	1746.6	1807.5	1828.2	1842.9	2099.7	2261.2
Banks Acceptances	3.4	4.2	4.3	6.2	3.2	3.5	4.2
Investments	190.1	188.6	173.5	144.6	188.1	172.8	165.7
Fixed Assets	218.3	224.4	225.9	237.3	243.9	252.8	255.9
Other Assets	250.4	236.0	249.3	197.3	213.2	208.7	220.9
Total Assets	7471.9	7308.3	7657.6	7640.4	7570.7	7755.0	8156.5
Deposits of PMA and Banks	660.4	466.0	456.2	442.9	417.6	426.4	383.6
Total Clients' Deposits	5424.7	5599.0	5873.6	5846.9	5772.5	5988.7	6385.9
Acceptances Executed & Outstanding	16.7	15.9	15.2	21.0	9.3	10.7	13.2
Other Liabilities	217.8	155.7	158.3	135.2	144.0	111.9	115.7
Provisions for Tax & Others	390.0	320.3	337.5	341.5	346.3	337.2	346.6
Equity	762.3	751.5	817.0	853.0	880.9	880.1	911.5
Total Liabilities	7471.9	7308.3	7657.6	7640.4	7570.7	7755.0	8156.5

Source: PMA - The consolidated budget of banks.

5.2 Bank Performance Indicators

The various indicators of the performance of Palestinian banks showed irregular growth by the end the 3rd quarter of 2009 as compared with the previous quarter. In

general, most indicators tended to rise. The credit facilities ratio to total deposits and to clients' deposits increased during this period by 0.7% and 0.3% respectively.

Table 22: Bank Performance Indicators 2006-2008 and the 1st – 3rd Quarters of 2009 (%)

Indicator	2006	2007	2008	Q1 2009	Q2 2009	Q3 2009
Net Income to Average Assets	1.0	1.1	1.2	1.4	1.63	1.54
Net Income to Average Equity	9.9	10.9	10.9	11.7	13.79	13.21
Credit Facilities to Total Deposits	39.5	29.8	29.1	29.8	32.7	33.4
Credit Facilities to Clients' Deposits	43.7	33.3	31.3	32.0	35.1	35.4
Private Sector Credit Facilities to Private Sector Deposits	35.4	27.8	24.7	24.1	24.6	26.6
Resident Private Sector Credit Facilities to Private Sector Deposits	34.1	26.9	22.8	22.3	23.3	25.4
Balances Abroad to Total Deposits	50.8	55.0	52.1	52.4	42.5	43.2
Clients Deposits to Total Assets	73.4	73.1	76.6	76.2	77.2	78.4
Credit Facilities to Total Assets	32.0	24.3	24.0	24.3	27.0	27.7

Source: PMA - The consolidated budget of banks.

The percentage of facilities extended to the private sector to those extended to the public sector also rose by 2.1% as well as the credit facilities proportion to total assets by 0.7%. In contrast, the end of the 3rd quarter of 2009 witnessed a slight decline in the ratio of net income to each of the average assets and average equity, where the first dropped by 0.1% and the second by 0.6% (see table 22).

5.3 Clearing House Activities

The data of the clearing house of the Palestinian Monetary Authority PMA show that there had been a rise in the number of checks presented for clearing as well as in their value by the end of the 3rd quarter compared to the previous quarter. The number of checks presented for clearing increased by nearly 9.8% during this period,

while their value increased by 3.6%. When these figures are compared to the 3rd quarter of last year, a rise of over 18.5% is revealed while their value is seen to have dropped by nearly 4%.

An increase is also noted in bounced checks, both in terms of number and value, by the end of the 3rd quarter of 2009 as compared to the previous quarter. The number of bounced checks increased by 1% from the rate registered in the previous quarter, amounting to 11.3%, while their value increased by about 1.5% reaching 6.9%. When these figures are compared to those of the corresponding quarter of last year, we notice a drop by about 0.5% in the number of bounced checks versus a rise of about 0.7% in their value by the end of the current quarter (see table 23).

Table 23: The Number and Value of Checks Presented for Clearing and the Number and Value of Bounced Checks (1st Quarter 2008 – 3rd Quarter 2009)

Period	Checks Presented for Clearing		Bounced Checks		Percent Bounced/checks presented for clearance	
	Number of checks	Value of checks (million \$)	Number of checks	Value of checks (million \$)	Number %	Value %
1 st Q 2008	603,281	1935.3	72,649	136.4	12.2	7.0
2 nd Q 2008	647,267	2144.3	72,762	132.4	11.2	6.2
3 rd Q 2008	686,097	2179.4	81,125	144.6	11.8	6.6
4 th Q 2008	717,579	2009.4	86,669	147.0	12.1	7.3
1 st Q 2009	668,531	1749.4	88,789	141.8	13.3	8.1
2 nd Q 2009	741,186	2016.6	76,523	109.2	10.3	5.4
3 rd Q 2009	813,545	2089.7	91,833	144.1	11.3	6.9

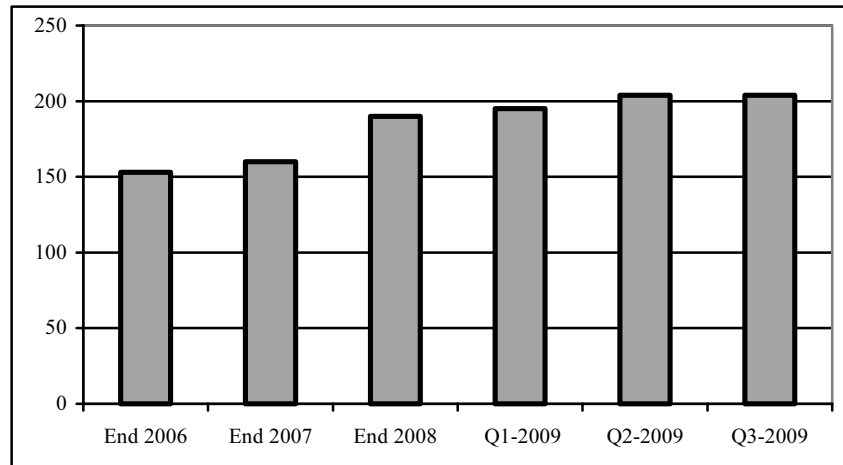
Source: PMA, Monthly Statistical Bulletin.

5.4 Number of Banks and Branches

There had been no change in the number of banks and branches by the end of the 3rd quarter of 2009 compared to the previous quarter. The number of banks remained 20, equally divided between local and foreign

banks. As for the number of branches and offices, there were still 204 branches and offices, divided by 99 branches and offices for local banks and 105 for foreign banks (see figure 11).

Figure 11: The Number of Branches and Offices of Banks Operating in the Palestinian Territories for 2006-2008 and the 1st - 3rd Quarter of 2009



Source: PMA.

6. Palestine Securities Exchange

Stock markets play a significant role in attracting the surplus and the non-employed capital in the national economy. They do this by transferring it from static capital into an active capital in the economic cycle, through investment in stocks and bonds traded by the Palestine Securities Exchange (PSE). Financial markets also provide real financial resources for companies issuing the stocks to finance their projects. This is in addition to the fact that stock markets motivate those companies to improve their economic performance and increase their profitability in order to maintain the prices of their stocks.

An important issue in this regard is the distinction between the efficiency of the stock market and that of the listed companies. The high price of the stocks of a certain company does not necessarily indicate the high efficiency of the market, as it may be attributed to an improvement in the profitability of the company or the leak of positive information in this regard. On the other hand, the efficient financial market is characterized by the rapid response of the prices of stocks of enlisted companies to any piece of new information received by dealers and that may change their perspective of the company issuing these

stocks. Stock prices tend to rise or fall depending on the nature of news whether positive or negative. In other words, a company's stock price in the efficient financial market reflects the available information about the company whether in the form of financial statements or as information pertaining to its activities transmitted by the media. The more rapid the response of the stock to information, the more efficient the market is. Thus in order to have an efficient financial market, information about the market must be available for all, at once, at no cost and with no restrictions on transactions such as taxes etc. This is in addition to the ability of the investor to sell and buy the number of stocks as he wants, easily and without any conditions. Also, there is a need for a large number of investors, numerous enough to prevent the impact on the prices of stocks as a result of the practices of some investors.

The following are the financial indicators usually used to monitor the reality and developments of the Palestine Securities Exchange:

1. Financial market size indicators:

- ◇ Market capitalization: it is measured by dividing the market value of shares

listed in the market by the GDP at current prices. This indicator is used to measure the importance and role of the financial market in the national economy. It is worth noting that this rate is calculated for the year as a whole and not by quarters.¹³ As the data for the year 2009 is available for 3 quarters only and at constant prices, the GDP was estimated for the year 2009 as a whole and at constant prices.¹⁴ Based on this, the market capitalization has been calculated and amounted to 48% in the Palestine Securities Exchange for the year 2009. In other words, the value of capital employed in the PSE is equivalent to almost half the value of the Palestinian production.

- ✧ The number of listed companies: this indicator points out the depth and diversity of the market. The number of companies listed in the Palestine Securities Exchange amounted to 38, 4 of which are suspended from trading. This number accounts for 30% of the total public shareholding companies operating in the Palestinian Territories.

2. Liquidity indicators:

- ✧ The value of traded shares to the GDP: this ratio amounted in PSE to 6.9% only in spite of the fact that the value of the shares listed reaches double the GDP. This means that the liquidity rate is modest in the Palestine Securities Exchange.
- ✧ Turnover: the turnover ratio is calculated by dividing the total value of shares traded by the total value of shares listed in the market. This amounted to 3.5% in the Palestine Securities Exchange. It is a very low

rate that may be attributed to the investors' fear of the unexpected volatility of prices or to the low percentage of speculators versus those who invest for the purpose of obtaining dividends or for saving. The highest turnover rate was recorded in the banking sector at 2.4%, followed by the investment sector (1.05%), insurance (0.98%), services (0.63%) and the least was in the industry sector (0.46%).

3. Volatility of returns indicators

Volatility of returns is measured through two main indicators: the coefficient of variation and the standard deviation of companies' returns. This indicator is used to determine the degree of financial stability of the listed companies. As the data on shares returns is not available in daily time-series for the 3rd quarter, it has been substituted by data on daily closing price for the largest companies in terms of trading size. The standard deviation for PalTel share price reached JOD 0.16, and \$0.15 for Bank of Palestine Ltd., JOD 0.09 for Palestine Industrial Investment Co., \$0.08 for Al Quds Bank, and \$0.02 for Padico.

4. Degree of concentration indicators

This is measured through the share of the largest five or ten companies in the value of stocks traded or listed in the securities exchange market. This indicator is used to determine the extent of impact of these companies on the changes in the securities exchange indices and most important, the stocks prices. In the Palestine Securities Exchange, the five largest companies captured 77.3% of the total shares traded. This is a high concentration that provides these companies with the capability to influence the PSE indices.

The following is a detailed review of the Palestine Securities Exchange Developments during the 3rd quarter of 2009. The number of shares traded dropped to 50.8 million compared to 54.6 million in the previous quarter and 91.2 million in the 1st quarter of the same year (see figure 12). This was coupled with a greater decline in

¹³ The market value of shares for a given quarter is the average of all months of the quarter. Hence, the value for the year is also the average for all months or quarters of the year while the GDP is the sum of the quarters. Therefore it is not possible to calculate the market capitalization for the quarter due the different basis for the calculation of the numerator (market value) than the denominator (GDP).

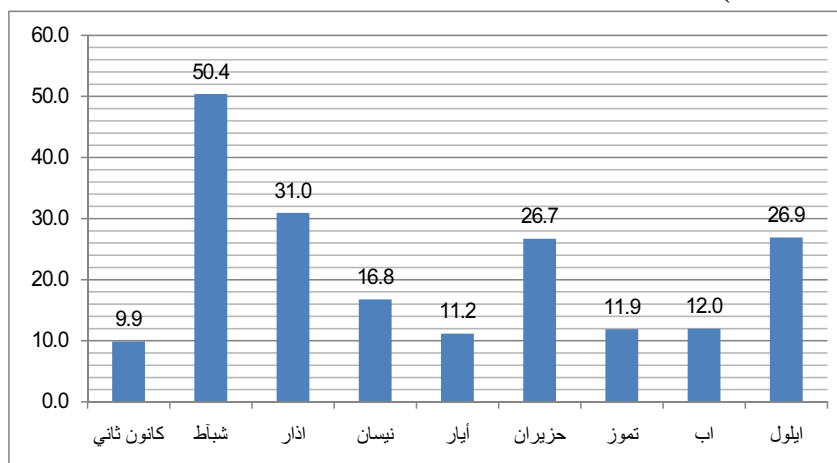
¹⁴ The GDP was calculated at constant prices for 2009 as follows: the sum of the first three quarters + the average of the first three quarters. Based on this equation, the GDP for 2009 amounted to \$4,895.7 million.

share value reaching \$80.6 million in the 3rd quarter compared to \$145.5 million in the 2nd quarter and \$189 million in the 1st quarter of the same year (see figure 13). The number of trading sessions has also declined

in the 3rd quarter to 61 sessions, 4 sessions less than the 2nd quarter and an increase of 1 session compared to the 1st quarter of the same year (see table 24).

Figure 12: The Number of Shares Traded in the Palestine Securities Exchange During the First 9 Months of 2009

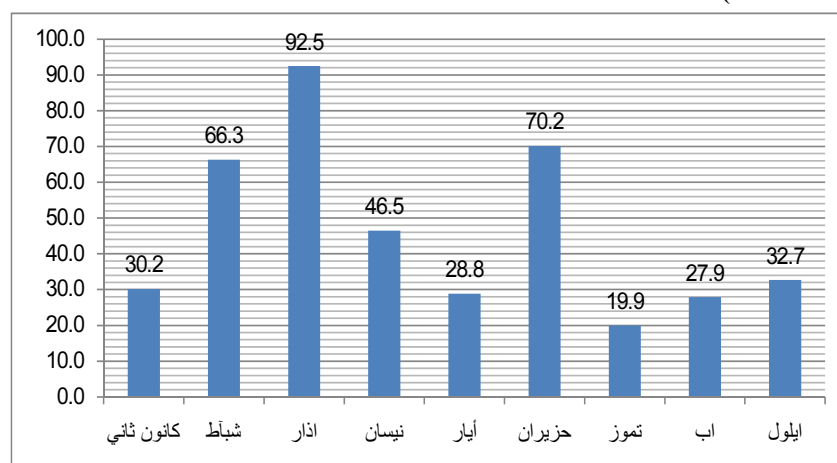
(USD million)



Source: The Palestine Securities Exchange. www.pse.com

Figure 13: The Value of Shares Traded in the Palestine Securities Exchange During the First 9 Months of 2009

(USD million)

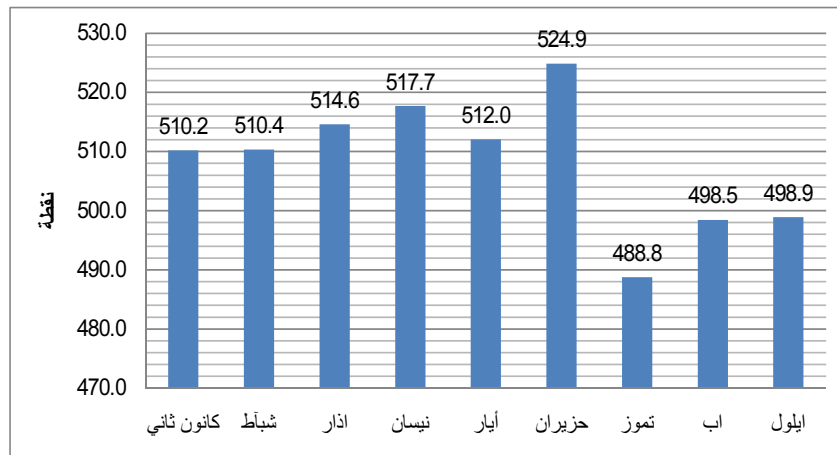


Source: The Palestine Securities Exchange. www.pse.com

With regard to prices, Al-Quds index declined by 4.9% at the end of the 3rd quarter of 2009 to reach 4,498.9 points compared to 524.9 points at the end of the 2nd quarter (see figure 14). The drop was obvious in the prices of the shares of the

services sector which reached 11.9%. The insurance sector shares also fell by 0.3%, in contrast to the banking and investment sector shares which increased by 9.5% and 2.4% respectively.

**Figure 14: Al-Quds (Jerusalem) Index
For the First 9 Months of 2009**



Source: The Palestine Securities Exchange. www.pse.com

On the level of corporation performance, data indicates that out of 34 companies trading their shares, the value of the shares of 24 companies dropped in July versus 9 companies that achieved a rise. In August, 10 companies suffered a loss in their share value versus 18 companies that achieved a

rise. September witnessed the least number of companies to experience a loss in their shares value, reaching 8 companies compared to 23 companies that achieved an increase. Apparently, the month of July was the worst with regard to the prices of traded shares, their number and total value.

**Table 24: Key indicators of the Palestine Securities Exchange
During the Months of the 3rd Quarter of 2009 and the Preceding Two Quarters**

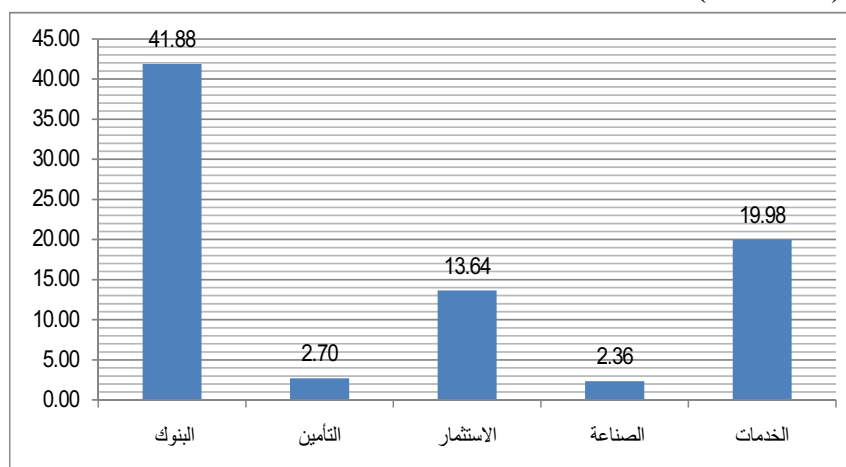
Period	Market capitalization (USD billion)	The number of trading sessions	Al-Quds Index, At the end of each month	Trading Volume (value of traded stocks) (USD million)	The number of traded stocks (USD million)
July	2.29	21	488.77	19.9	11.9
August	2.33	22	498.45	27.9	12.0
September	2.36	18	498.92	32.7	26.9
Q3 2009	2.33	61	498.92	80.6	50.8
Q2 2009	2.38	65	524.85	145.5	54.6
Q1 2009	2.40	60	514.61	189	91.2

Source: The Palestine Securities Exchange

With regard to sectors, the banking sector captured the lion's share of traded shares in the PSE during the 3rd quarter of 2009, at a value of \$41.9 million comprising 52% of the total value of shares traded in the market. The services sector follows at the value of \$19.9 million (24.8%), followed by the investment sector, worth \$13.64 million (16.9%) and the insurance sector worth \$2.7 million (3.3%). Whereas the industrial sector comes last at a value of \$2.36 million (2.9%) (See figure 15).

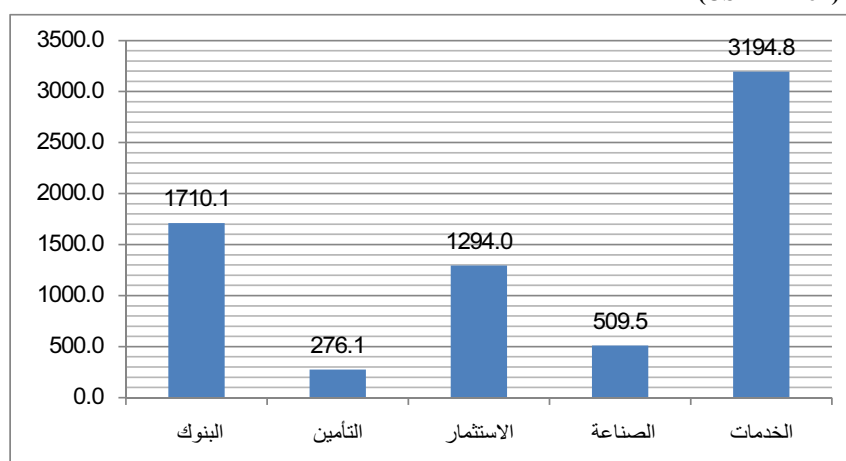
Although the share of the services comes second in terms of the value of shares traded, it ranks first in terms of shares listed in the market amounting to \$3.2 billion and comprising 45.7% of the total listed shares. The banking sector follows at the value of \$1.7 billion (24.5%). This proves once again that the turnover rate in the bank sector is higher than in the service sector. The investments sector ranks third at the value of \$1.3 billion (18.5%), then comes the industry sector at the value of \$509.5 million (7.3%) and the least is the insurance sector at the value of \$276.1 million (3.9%) (See figure 16).

Figure 15: The Value of Shares Traded in the Palestine Securities Exchange by Sector for the 3rd Quarter of 2009
(USD million)



Source: The Palestine Securities Exchange. www.pse.com

Figure 16: The Value of Shares Listed in the Palestine Securities Exchange by Sector for the 3rd Quarter of 2009
(USD million)



Source: The Palestine Securities Exchange. www.pse.com

7. Prices and Purchasing Power¹⁵

Tracking the Consumer Price Indices - CPI in the Palestinian Territories shows an increase in the 3rd quarter of 2009 compared to the previous quarter. This increase in the CPI is a continuation to the increase that

occurred in the 2nd quarter of 2009. But, this increase remains limited when compared to the sharp rise during the 2008 quarters.

¹⁵ The Palestinian Central Bureau of Statistics updated the base year in the calculation of the base figure for consumer prices in accordance with international recommendations. A change was made in the year from 1996 to 2004. That year was chosen on the basis that it was the most stable of the *Al-Aqsa Intifada* year, the measurements of which were studied. Another classification of goods, the 'classification of individual consumption according to purpose' set by the European Union (COICOP), was used. It depends on classification of the groups to 12 main groups, instead of 10, in addition to changing the distribution of certain goods inside some groups in a new way which depends on classification of goods according to the purpose of use.

7.1 Prices

With the persistent recession in the wave of increases in international prices, especially with the stabilization in the prices of basic food commodities and in addition to the decline in oil prices and their stability at a relatively moderate price, the CPI in the Palestinian Territories witnessed a slight rise in the 3rd quarter of 2009. The CPI increased from 123.03 in the 2nd quarter of 2009 to 125.37 in the 3rd quarter of 2009 (see table 25). It is noted that the group that has most affected the CPI during the 3rd quarter is the food stuff and refreshing beverages group, at 2.12%, which in its turn was affected by the rise in the prices of fresh fruits & vegetables, sugar and non alcoholic beverages. In addition, the prices of alcoholic beverages and tobacco increased by 4.85% due to the rise in the prices of cigarettes.

The prices of the housing and its accessories group increased by 2.22%, influenced by the rise in the prices of gasoline and domestic liquid fuel. The group of educational service prices increased by 2.87% as a result of the rise in tuition fees. The prices of the textiles, apparels and footwear group increased by 1.61% as well as the prices of the furniture, furnishing and house goods group by 1.88%. On the other hand, the prices of various goods and services group registered a slight drop by 0.22%. Moreover, the increase in the prices of most essential commodities has receded, in particular flour, bread, oil, rice and fresh meat. With regard to the rest of the groups, they recorded a slight increase in their average prices during the 3rd quarter compared to the 2nd quarter of 2009 (see table 26).

Table 25: The CPI and its Monthly and Quarterly Percentage Changes in the Consumer Prices in the Palestinian Territories During the 2nd & 3rd Quarters of 2009 Base year 2004 (2004=100)

Time Period	CPI	Monthly Percentage Change (%)	Quarterly Percentage Change (%)
April 2009	122.55	(0.21)	
May 2009	123.05	0.40	
June 2009	123.48	0.35	
2nd Quarter Average	123.03		0.86
July 2009	124.22	0.60	
August 2009	125.60	1.11	
September 2009	126.28	0.54	
3rd Quarter Average	125.37		1.90

Source: Palestinian Central Bureau of Statistics, 2009

With regard to Palestinian regions, the prices in the West Bank witnessed an increase by 2.28% during the 3rd quarter compared to the previous quarter, while it witnessed a decline by 0.28% compared to the corresponding quarter of 2008. In Jerusalem, the prices registered an increase by 2.04% compared to the previous quarter

and by 3.31% compared to the corresponding quarter of 2008. As for the Gaza Strip, the CPI indicates an increase in prices by 1.04% during the 3rd quarter of 2009 compared to the previous quarter of the same year, and an increase by 2.46% compared to the corresponding quarter of 2008.

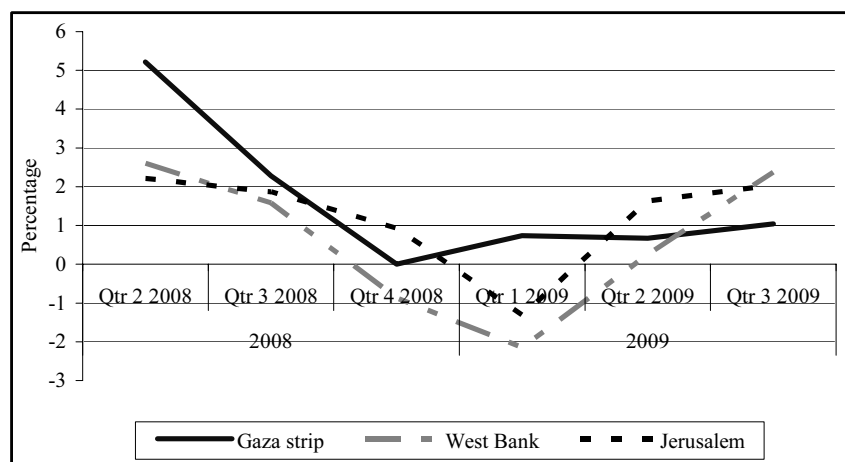
Table 26: Average Change in CPI by Main Commodity Categories in the Palestinian Territories in the 3rd Quarter of 2009 Compared to the Previous Quarter and the corresponding Quarter of 2008 Base year 2004 (2004=100)

Group	Q3/2009 over Q2/2009 Percentage Changes	Q3/2009 over Q3/2008 Percentage Changes
Food Stuff and Refreshing Beverages	2.12	2.06
Alcohol Beverages and Tobacco	4.85	13.38
Textiles, apparels and footwear	1.61	4.25
Housing and related items	2.22	(1.56)
Furniture and house goods and appliances	1.88	6.45
Healthcare	0.36	(0.82)
Transportation and Travel	2.23	(4.22)
Telecommunication	0.24	0.57
Recreational and Cultural goods and services	0.30	1.78
Education services	2.87	4.30
Restaurants, Cafes and Hotels Services	0.74	2.76
Various good and services	(0.20)	3.99
General CPI	1.90	1.95

Source: the PCBS, Price Surveys 2008-2009.

Figures in brackets indicate a negative value (decline in prices).

Figure 17: Shekel-based Inflation Rate in Jerusalem, the West Bank and the Gaza Strip By Quarters 2nd 2008 – 3rd 2009



Source: calculations based on the PCBS data, the Consumer Price Index (CPI), various issues.

Now a look at the regions and the different groups of the consumer basket in the Palestinian Territories. It is noted that the alcohol beverages and tobacco group witnessed an increase by 5.61% in Jerusalem during the 3rd quarter of 2009 compared to previous quarter, while it increased by 6.34% in the West Bank and by 3.17% in the Gaza Strip. The transportation and travel group recorded a

rise that reached 2.5% in the West Bank during the 3rd quarter of 2009. It also recorded an increase in Jerusalem and the Gaza strip by 1.38% and 3.26% respectively. The decline in prices had affected several groups in the West Bank and a fewer number of groups in the Gaza Strip, while no decline was recorded in any of the groups in Jerusalem (see table 27).

Table 27: Changes in the CPI in the Palestinian Territories by Region and Commodity Group in the 3rd Quarter of 2009 Compared to the Previous Quarter

Group	West Bank (%)	Gaza Strip (%)	Jerusalem (%)
Food and soft drinks	3.47	0.67	1.68
Alcoholic beverages and tobacco	6.34	3.17	5.61
Textiles, clothing and Footwear	(0.10)	1.20	2.56
Housing & related items	2.01	1.11	2.28
Furniture, household goods	(0.74)	3.15	2.86
Medical care	0.41	(0.73)	0.66
Transportation	2.50	1.38	3.26
Communication	(0.09)	0.51	0.28
Recreational cultural goods and services	(1.17)	(0.03)	2.07
Education	4.22	2.27	1.45
Restaurants and Cafes Services	0.80	1.32	0.68
Miscellaneous goods and services	(1.71)	(0.06)	0.43
General CPI	2.28	1.04	2.04

Source: the PCBS.

Figures in brackets indicate a negative value.

7.2 Average Prices of Selected Consumer Goods

Prices of certain consumer goods witnessed varying changes during the 3rd quarter of 2009. Following is a review of price movements for selected groups of goods during the 3rd quarter of 2009, compared to the previous quarter:

Fuel prices:

Prices of the group of fuel used for cars witnessed an increase of 11.29% during the 3rd quarter compared to the 2nd quarter of 2009.

Fresh Fruits prices:

Prices of the fresh fruits group recorded a rise by 12.22% during the 3rd quarter of 2009.

Vegetables prices:

The prices of the vegetables group recorded an increase by 14.62% during the 3rd quarter of 2009.

Sugar prices:

The sugar group prices have risen of 5.83% during the 3rd quarter of 2009.

Cigarettes prices:

The cigarettes group recorded a rise of 4.96% during the 3rd quarter of 2009.

Rice prices:

The rice group prices registered a slight rise of 0.30% during the 3rd quarter.

Flour prices:

The prices of the flour group listed a drop of 3.35% during the 3rd quarter of 2009 compared to the 2nd quarter.

Fresh meat prices:

The prices of the fresh meat group registered a decline of 0.52% during the 3rd quarter of 2009.

Fresh chicken prices:

The fresh chicken group prices recorded a drop of 2.19% during the 3rd quarter of 2009 compared to the 2nd quarter of 2009.

Oil and fat prices:

The prices of the oil and fats group recorded a decline of 1.25% during the 3rd quarter of 2009 compared to the 2nd quarter of 2009.

Dairy products and eggs prices:

The prices of dairy products and eggs group registered a drop of 3.15% during the 3rd quarter of 2009.

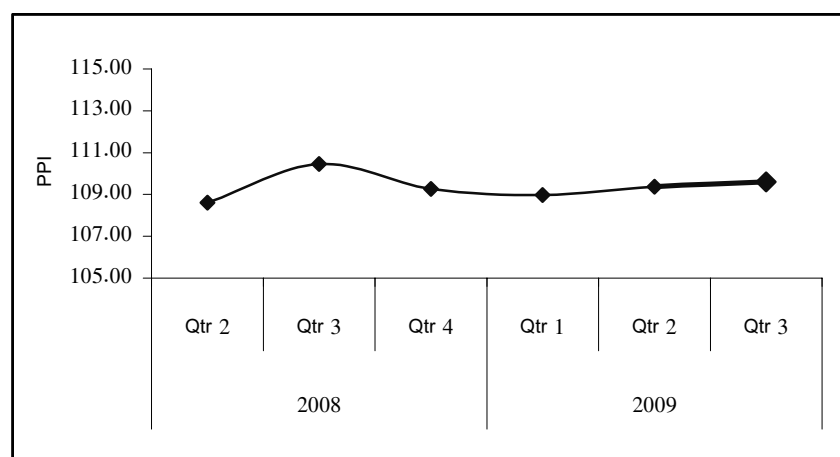
7.3 Producer Prices

Producer prices are the prices received by a producer from a buyer in exchange for a certain commodity, minus the value added tax (VAT), or any other deductible tax recorded on a buyer's receipt, excluding transportation costs. The producer prices

recorded a slight increase in the index figure by 0.22% during the 3rd quarter of 2009 compared to the 2nd quarter of 2009. The average CPI had risen from 109.37 during the 2nd quarter to 109.61 during the 3rd quarter (base year 2007=100) (see figure 18). This resulted in an increase in produced goods, prepared for sale to the activities of the manufacturing industry by 0.10%, whose relative importance constitutes 63.48% of the basket of producer prices. The prices of metallurgical and extracting industries witnessed an increase of 1.03%, its relative importance constitutes 1.26%.

Also, the prices of agricultural goods recorded a rise by 0.42%, its relative importance constitutes 35.06%. The prices of fishery increased slightly by 0.04%, its relative importance constitutes 0.20%. The main reason for the rise in the principal activities is attributed to the rise in the prices of both the locally produced commodities and the exported commodities by 0.21% and 0.29% respectively. When compared with the corresponding quarter of 2008, the average producer prices recorded a rise of 0.77%.

Figure 18: The General Direction of the Movement of the Producer Prices Indices (PPI) In the Palestinian territories for the Quarters: 2nd 2008 – 3rd 2009 (Base year 2007=100)



Source: the PCBS.

The PCBS updated the base year used for the calculation of producer prices index in line with the international recommendations from the year 1996 to 2007.

7.4 Currency Exchange Rates

The exchange rate of the USD continued to fall against the NIS during the 3rd quarter of 2009, losing more of its value after the relative improvement it had witnessed in the

first two quarters of the year. The cumulative sum total of the loss in the USD value against the NIS amounted to 4.1% during the 3rd quarter of 2009.

Table 28: Average Monthly Exchange Rate of USD and JOD against the NIS October 2008 - September 2009

Month	US Dollar		Jordanian Dinar	
	Average Exchange Rate	Percentage Change (%)	Average Exchange Rate	Percentage Change (%)
October 2008	3.67	3.88	5.17	3.75
November 2008	3.87	5.55	5.47	5.68
December 2008	3.82	(1.32)	5.44	(0.51)
January 2009	3.90	1.91	5.50	1.08
February 2009	4.10	5.29	5.77	4.92
March 2009	4.16	1.34	5.87	1.71
April 2009	4.18	0.5	5.90	0.5

Month	US Dollar		Jordanian Dinar	
	Average Exchange Rate	Percentage Change (%)	Average Exchange Rate	Percentage Change (%)
May 2009	4.07	(2.6)	5.75	(2.5)
June 2009	3.98	(2.2)	5.57	(3.1)
July 2009	3.90	(0.73)	5.50	(1.22)
August 2009	3.83	(1.8)	5.40	(1.8)
September 2009	3.77	(1.54)	5.32	(1.54)

Source: the PMA.

* Figures in brackets indicate negative value.

Values were calculated according to the monthly average exchange rate for buying and selling.

As the JOD is pegged to the USD with a fixed exchange rate system, the loss in the value of the JOD vis-à-vis the NIS is very close to the value lost by the USD, where the cumulative sum total of the loss in the JOD value during the same period is about 4.5%.

7.5 Purchasing Power

The drop which occurred in the exchange rate of both the US Dollar and Jordanian Dinar vis-à-vis the NIS reflected directly on

the purchasing power of the two currencies, being among the currencies used in the Palestinian market. During the 3rd quarter of 2009, the total purchasing power decline amounted to 6.31% for the USD and 8% for the JOD. So the purchasing power of both currencies retreated during the 2nd and 3rd quarters of the year by about 12.6% and 13.8% respectively. This means the two currencies lost again the rise achieved during the 1st quarter of 2009 (see table 29).

Table 29: Average Monthly Exchange Rates (USD & JOD against NIS) and Changes in their Purchasing Power January – September 2009

Month	Percentage Change in the CPI (%)	Currency	Percentage Change in the Currency Exchange Rates (%)	Percentage Change in the Purchasing Power of the Currency (%)
January 2009	(0.71)	USD	1.91	2.63
		JOD	1.08	1.79
February 2009	(0.02)	USD	5.29	5.31
		JOD	4.92	4.94
March 2009	1.05	USD	1.34	0.29
		JOD	1.71	0.66
April	(0.22)	USD	0.60	0.82
		JOD	0.45	0.67
May 2009	0.41	USD	(2.73)	(3.14)
		JOD	2.57)	(2.98)
June 2009	0.35	USD	(3.58)	(3.93)
		JOD	(3.09)	(3.44)
July 2009	0.60	USD	(0.73)	(1.33)
		JOD	(1.22)	(1.82)
August 2009	1.11	USD	(1.79)	(2.90)
		JOD	(1.80)	(2.91)
September 2009		USD	(1.54)	(2.08)
		JOD	(1.54)	(2.08)

Source: PMA, PCBS.

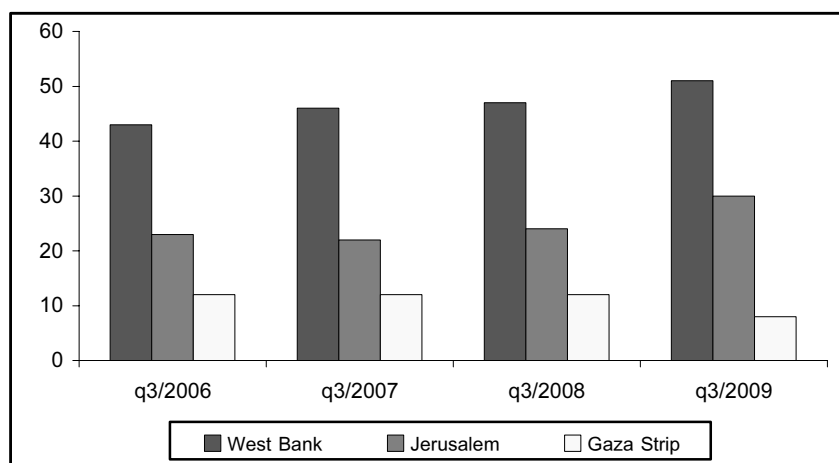
* Figures in brackets indicate negative value.

8. Hotel Activity

Tourism activity in the Palestinian Territories witnessed some improvement since the beginning of 2007. In the 3rd quarter of 2009 the hotel activity recorded a rise in the number of guests compared to the corresponding quarter of the previous year. The tourism sector continues to suffer from fluctuations and instability as a result of Israeli arbitrary practices and various security troubles.

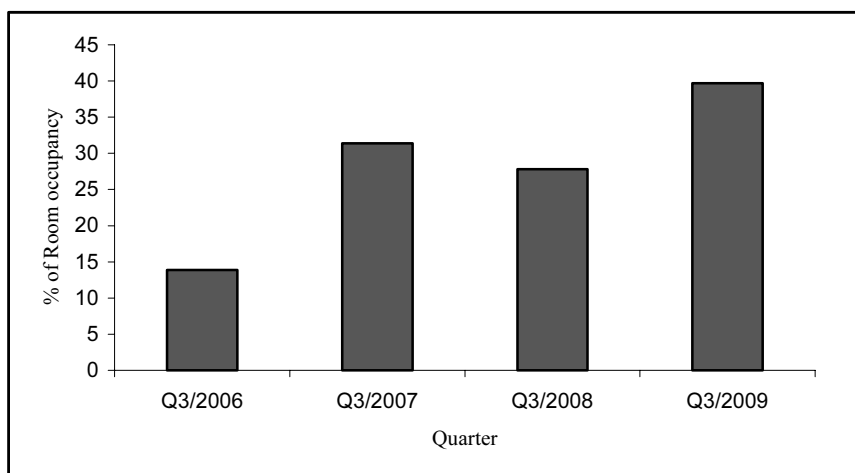
The total number of hotels in the Palestinian Territories reached 120, including those operating and temporarily closed (see figure 19). The number of operating hotels changes according to the month of the year. In September 2009, there were 89 operating hotels which had 4,666 rooms, having a total of 10,238 beds. The number of guests in the Palestinian Territories hotels totaled 135,939 guests during the 3rd quarter of 2009, 14.7% of them were Palestinians and 34.4% from the European Union.

Figure 19: Number of Operating Hotels in the Palestinian territories By 3rd Quarters, 2006-2009



Source: PCBS, 2009, Hotel Activity in the Palestinian Territories, 3rd Quarter 2009.

Figure 20: Hotel Room Occupancy Rates during the 3rd Quarters, 2006-2009



Source: PCBS, 2009, Hotel Activity in the Palestinian Territories, 3rd Quarter 2009.

The average room occupancy in operating hotels in the PT reached 1,825.6 hotel rooms daily, i.e. 39.7% of available rooms (see figure 20). Hotel guests concentrated in hotels in Jerusalem, reaching a percentage of 50.6% of the total number of guests. This was followed by the hotels in the south and centre of the West Bank, where the percentage reached 25.8% and 21.4% respectively. The percentage of guests in hotels in the north of the West Bank was 2.1%, while it was 0.1% in hotels in the Gaza Strip.

The number of nights spent in hotels in the Palestinian Territories totaled 310,643 nights during the 3rd quarter of 2009, where the total number of nights for Palestinian guests constituted 15.6% and 36.7% for the guests from the European Union. The

percentage of guests from the USA and Canada was 10.8%. In comparison with the corresponding quarter of 2008, a rise is realized in the number of nights spent in hotels reaching 30.3% compared with an increase of 29.0% in the previous quarter of 2009.

The average length of stay in hotels in the Palestinian Territories was 2.3 nights per guest during the 3rd quarter of 2009. The highest average length of stay was 2.7 nights per guest in the south of the West Bank. In the north and center of the West Bank, the average was 1.7 and 2.0 nights per guest, respectively. In Jerusalem, the average length of stay in hotels amounted to 2.2 nights per guest and to about 1.5 nights per guest in the Gaza Strip (see table 30).

Table 30: Percentage Change in Hotel Activity Indicators during the 3rd Quarter of 2009 Compared to the Previous Quarter and the Corresponding Quarter of 2008

Indicator	Percentage Change Over the Q3/2008	Percentage Change Over the Q2/2009
Number of Operating Hotels at the End of the Quarter	4.7	(2.2)
Average Number of Employees During the Quarter	5.0	2.2
Number of Hotel Guests	42.0	37.0
Number of Nights Accommodation	30.3	29.0
Average Rooms Occupancy	38.9	44.3
Average Beds Occupancy	30.3	27.6
Rate of Rooms Occupancy (%)	42.8	34.6
Rate of Beds Occupancy (%)	27.7	17.0

Source: PCBS, 2009, Hotel Activity in the Palestinian Territories, 3rd Quarter 2009.

* Figures in brackets indicate negative value.

9. Investment Indicators

9.1 Company Registration

There are two different company laws in effect in the Palestinian Territories. While the Jordanian Companies Law Number (12) of 1964 is applied the West Bank, there are two company laws applicable in the Gaza Strip. This includes the Companies' Law number (18) of the year 1929 and the Ordinary Companies' Law number (19) of the year 1930, where the Ministry of National Economy registers companies in accordance with these laws.

The economic monitor analyzes the data on companies in terms of the number of companies registered, their types and registered capital. A sectoral analysis of the registered companies and their legal status is also undertaken. According to the legal status, companies are classified into three types: shareholding companies (public and private), ordinary companies, and foreign shareholding and ordinary companies. This is in addition to company classification by geographic area. The Monitor concludes,

from analyzing company statements, a preliminary idea about the course of investment activities and the economy's ability to attract domestic and foreign capital.

The number of registered companies in the West Bank witnessed a drop of about 15% during the second quarter of 2009 compared to the previous quarter, where 349 companies were registered during the period from the end of June until the end of September, compared to 412 companies during the previous quarter (see table 31). Despite this drop, the number of registered companies during the 3rd quarter of 2009 remains higher than its level during the corresponding quarter of 2008, which also witnessed a drop in the number of registered companies at that time, but it was less than the number of companies registered during

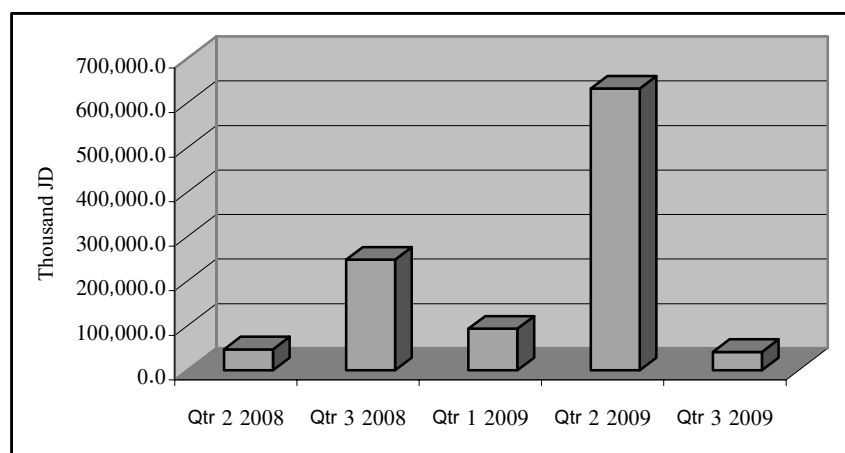
the 1st and 2nd quarters of 2009. The registered capital had also dropped with the drop in the number of registered companies, but it was big and reached more than 93%. The reason for this is that the previous quarter witnessed the registration of companies with very big capital, raising the total capital of registered companies during that quarter. Moreover, the vast majority of the companies registered during the 3rd quarter (76.5%) were those with capitals of \$100 thousand or less. Thus, the registered capital declined to JOD 41.1 million. It is worth mentioning that the Ministry of National Economy has no information pertaining to the registration of companies in the Gaza Strip during the 3rd quarter of 2009 (which has been the case since November 2007).

Table 31: Development of the Number of New Companies Registered In the West Bank during the Quarters: 2nd Q 2008 – 3rd Q 2009

Number of Companies	Quarter
334	Q2, 2008
315	Q3, 2008
287	Q4, 2008
454	Q1, 2008
412	Q2, 2009
349	Q3, 2009

Source: Ministry of National Economy, Department of Company Registration, 2008 and 2009.

Figure 21: Capital Value for New Companies Registered in the West Bank in JOD for the Quarters: 2nd Q 2008 – 3rd Q 2009

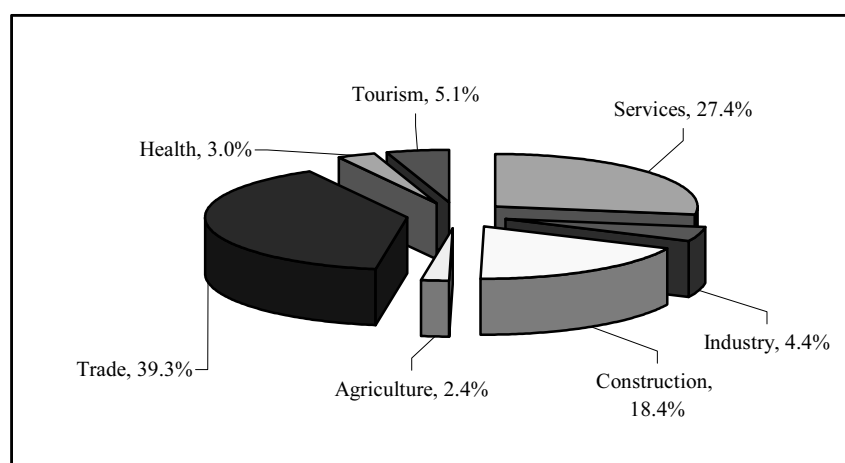


Source: Ministry of National Economy, Department of Company Registration, 2008 and 2009.

The 3rd quarter of 2009 witnessed a big change in the shares of the different economic sectors with regard to registered capital in the West Bank. Figure 23 shows a decline in the share of the services sector in the capital of newly registered companies by over a half, thus capturing 27.4% and ranking second after the trade sector, whose acquisition of shares in registered capital increased largely to reach 39.3% compared to 1.39% during the previous quarter. It was also noted that the share of construction had

dropped and it ranked third after the services sector. The share of this sector dropped from 26.5% to 18.4% during the 3rd quarter while the remaining sectors still acquire the least shares in registered capital as follows: The health sector 3%, the industry sector 4.4%, tourism around 5% and the share of the agriculture sector was the lowest at 2.4%, registering 4 companies only in the 3rd quarter of 2009 (see figure 22).

Figure 22: Distribution of Capital for Newly Registered Companies in the West Bank by Economic Activity During the 3rd Quarter of 2009 (%)



Source: Ministry of National Economy, Department of Company Registration, 2009.

The companies' data is not considered an indicator of investment only, but also of the trends and the legal status of companies in the Palestinian Territories. Looking at the legal status of registered companies during the 3rd quarter of 2009, we notice a clear change in distribution of capital on the different types of companies, compared to the previous quarter. During this quarter, only 1 foreign private shareholding company was registered. Thus, its share dropped to reach only 0.7% of the total capital registered in this quarter, compared to 66.1% during the previous quarter. The share of private shareholding companies increased to 55.6% compared to 31.5% in the previous quarter. The share of the ordinary companies also increased from 2.4% during the previous quarter to 43.7% during this quarter. This occurred while no public shareholding company, foreign ordinary company, foreign public

shareholding company or ordinary limited company was registered during the 3rd quarter of 2009.

On the other hand, it is noted that most of the new companies registered in the West Bank are concentrated in the Ramallah, Al-Bireh and Nablus governorates. During the 3rd quarter of 2009, the percentage of new companies registered in Ramallah and Al-Bireh governorates dropped from 37% to 28.2%. Following this comes the Nablus and Hebron governorates, where the share of registered companies during the 3rd quarter was 22.1% and 15.5% respectively with an increase in comparison to the previous quarter. Both Hebron City and the City of Nablus are surrounded by urban population centers which explain the high percentage of companies registered in these communities to the total number of companies registered in the Governorate.

Table 32: The Distribution of Capital for Newly Registered Companies in the West Bank by Legal Classification during the 3rd Quarters of 2008 and the First 3 Quarters of 2009

(JOD)

Total	Ordinary Limited	Foreign Public Shareholding	Foreign Ordinary	Legal Form			Public Ordinary	Year
				Foreign Private Shareholding	Public Shareholding	Private Shareholding		
248,465,527	0	0	150,000,000	6,311,527	0	73,977,500	18,176,500	Q3 2008
93,431,250	100,000	0	0	1,603,770	0	69,548,440	22,179,040	Q1 2009
625,707,008	0	0	0	413,528,125	0	197,102,459	15,076,424	Q2 2009
41,183,340	0	0	0	300,000	0	22,895,540	17,987,800	Q3 2009

Source: The Ministry of National Economy, Department of Company Registration, 2009.

The Jenin Governorate shares the previously mentioned feature with each of the Hebron and Nablus governorates. Despite the fact that the number of its inhabitants is less than the other governorates, there is an increased economic strength in the city's surroundings due to the relatively good development of the infra-structure available for the communities surrounding the city. This has contributed to the variety of projects in the governorate which raised the percentage of registered companies to 14.7%, especially when compared to the number of newly registered companies in neighboring governorates which possess an agricultural economy similar to that of Jenin. The

governorates of Tulkarem, Qalqilya and Salfit obtained a percentage of 0.7%, 2.7% and 1.0%, respectively, of the newly registered companies (see table 33).

As for newly registered companies in the suburbs of Jerusalem, they were 3.3% of the total number of newly registered companies. Whereas the percentage of newly registered companies in the Bethlehem governorate was 9.4%, it was 2.4% in Jericho and the Jordan Valley governorate, which is characterized by an agricultural nature that limits the possibilities of investment in other sectors (see table 33).

Table 33: The Distribution of the Newly Registered Companies in the West Bank By Governorates during the First 3 Quarters of 2009

Governorate	Q1 2009	Percent to Total %	Q2 2009	Percent to Total %	Q3 2009	Percent to Total %
Ramallah and Al-Bireh	144	31.7	152	37.0	123	28.2
Hebron	91	20.0	58	14.1	51	15.5
Nablus	66	14.5	63	15.3	71	22.1
Tulkarem	22	4.8	19	4.6	4	0.7
Jenin	57	12.6	42	10.2	47	14.7
Jericho & the Jordan Valley	7	1.5	7	1.7	6	2.4
Jerusalem Suburbs	18	4.0	12	2.9	14	3.3
Bethlehem	33	7.3	35	8.5	19	9.4
Qalqilya	9	2.0	10	2.4	10	2.7
Salfit	7	1.5	13	3.2	4	1.0
Total	454	100	412	100	349	100

Source: The Ministry of National Economy, Department of Company Registration, 2009.

9.2 Building Licenses

Building licenses, issued during a certain period of time, are considered an indicator of investment activity in the construction

sector, taking into account that the number of issued licenses does not include all building activities in the construction sector.

The reason is that a part of building activities, especially in the rural areas, are not registered and no licenses are issued for these buildings.

The number of issued building licenses is greatly affected by climatic and environmental factors during a given period of time. Consequently, the increase and decrease in the number of licenses can be noted during the different seasons of the year. Activities related to the building and construction sector increase during the second and third quarters (during the summer season), whereas the volume of such activities decreases during the first and fourth quarter (during the winter season). This connection with the previously mentioned factors makes comparison, between the number of permits issued during a certain quarter and those issued during its corresponding quarter in a previous year, more meaningful and accurate.

Statistics of building licenses point to a decrease in their number during the 3rd quarter of 2009, compared to the corresponding quarter of 2008, by 18.2%. No statistics are available for the Gaza Strip for the 3rd quarter of 2009 which was the case for the 1st, 3rd and 4th quarters of 2008, as well as the 1st and 2nd quarters of 2009.

The total area of licensed buildings during the 3rd quarter of 2009 was nearly 510.2 thousand sq. m., with an increase of nearly 11.2% over the corresponding quarter of 2008. The number of housing units witnessed a substantial increase during the 3rd quarter of 2009. Whereas the number of licensed housing units during the 3rd quarter of 2008 was around 1,174 units, it had risen to 1,311 units, an increase of 11.7%, and consequently the area of those units increased by 3.0%. The number of existing licensed dwellings has also risen to 495 units, an increase of nearly 41.6% (see table 34).

Table 34: Some indicators for Building Licenses and Licensed Areas in the Palestinian Territories during the Quarters: 2nd Q 2008 – 3rd Q 2009

	Q2 2008	Q3 2008*	Q4 2008*	Q1 2009*	Q2 2009*	Q3 2009
Total Licenses Issued	1,155	1,096	980	1,219	1,309	1,296
Residential Building	979	931	827	1,052	1,144	1,135
Non-residential Building	176	165	153	167	165	161
Total Area Licensed (Thousand Sq. m.)	354.8	458.8	385.5	469.2	522.9	510.3
New Units	1,062	1,174	1,111	1,266	1,485	1,311
Area (Thousand Sq. m.)	195.2	234.3	195.5	245.6	311.2	241.4
Existing Units Numbers	331	223	202	261	322	495
Area (Thousand Sq. m.)	60.7	62.5	51.6	74.3	85.6	88.5

Source: The PCBS (2009). Statistics of Building Licenses, Ramallah - Palestine.

* The data for these quarters is for the West Bank only and does not include the Gaza Strip.

10. Expectations of Owners and Managers of Industrial Establishments

10.1 General performance of industrial establishments

19.2% of the owners and managers of industrial establishments found that the general performance of their establishments improved during September 2009 compared to August of 2009 (19.1% in the West Bank and 22.3% in the Gaza Strip).

10.2 Production

The rise in prices and costs of raw materials was the main factor affecting the costs of production according to 91.4% of the owners and managers of industrial establishments in the Palestinian Territories,

92.3% in the West Bank and 77.8% in the Gaza Strip. 88.4% of the owners and managers of industrial establishments pointed to the great influence of the current political conditions, 88.8% in the West Bank and 83.4% in the Gaza Strip. 80.4% of the owners and managers of industrial establishments also pointed to the impact of transportation expenses on production costs (82.6% in the West Bank and 44.5% in the Gaza Strip).

10.3 Employment

9.5% of the owners and managers of industrial establishments in the Palestinian Territories indicated that they had laid-off workers during September 2009 (9.7% in the West Bank and 5.6% in the Gaza strip). 78.8% pointed that no change occurred in the number of workers (78.3% in the West Bank and 88.8% in the Gaza Strip). The expectations of the owners and managers of industrial establishments with regard to employment during October 2009 show that only 20.4% of them expect a rise in the level of employment (20.7% in the West Bank and 16.7% in the Gaza Strip).

With regard to the expectations of the owners and managers of industrial establishments in the medium term (i.e. during the next six months), the expectations indicated that 26.6% expect a rise in the level of employment in the Palestinian Territories (26.6% in the West Bank and 27.8% in the Gaza Strip).

10.4 Financial conditions and financing by borrowing

The survey results show a weak demand on loans from the banks operating in the Palestinian Territories by industrial establishments during the 3rd quarter of 2009. 93.6% of the owners and managers of industrial establishments indicated that they did not request loans from operating banks (93.3% in the West Bank and 100% in the Gaza Strip). 5.8% of the operating industrial establishments that submitted a request for loans did so only once against the other establishments that resorted to borrowing from banks 2-5 times.

As for future expectations for the month following September 2009, 35.8% of owners and managers of industrial establishments expect an improvement in their financial conditions and 4.0% only expect improvement in bank facilities.

11. Israeli Measures¹⁶

11.1 The Martyrs and Injured

The number of martyrs was 29 during the second half of 2009, 6 of them were children. 4 resistance militants were assassinated in the Nablus governorates in December 2009. The number of wounded Palestinians during the same period was 273 persons; including 40 children, 3 women, 5 foreign supporters and 4 journalists. The number of detainees in all the Palestinian Territories was 1,468 persons, 98% of them from the West Bank.

11.2 Obstacles to Movement and Travel

The number of Israeli military road blocks that are mounted abruptly (temporary check posts) in the West Bank was 2,499 road blocks during the second half of 2009. The number of total closures of crossing points during the same period was 846. Crossing points with the Gaza Strip and Israel were closed 175 times and international border crossing points were closed 99 times. The Israeli occupation forces kept many permanent road blocks, which have added to the sufferings of citizens because of the complicated passage formalities. These include strict searching, interrogation, and delays that last hours. The total closure of those crossing points is sometimes due to alleged security measures, which resulted in dividing the West Bank and isolating its northern part from the center, and the center from the southern part. It has made movement between Palestinian cities and towns a very strenuous task.

¹⁶ Monthly report of the Palestinian Control Group (July, August, September, October, November, December 2009). Website of the Palestinian Control Group: <http://www.nad-plo.org>.

11.3 Assaults on Education and Health Sectors

There were 13 Israeli assaults against the Palestinian education sector during the second half of 2009. Those assaults included the threat of closing down a school and the inspection of two other schools in the Qalailia governorate, in addition to turning a school into an interrogation center in the Ramallah governorate. As for the health sector, it was exposed to 3 assaults in the West Bank and 3 in the Gaza Strip during the second half of 2009, and included the prevention of two ambulances from reaching their destinations and firing at other ambulances.

11.4 Assaults on Property and House Demolitions

Targeting public and private Palestinian properties by the Israeli occupation authorities continued. The Israeli occupation forces occupied 33 houses during the second half of 2009, to be used for military purposes for varying periods of time. The assaults on Palestinian property amounted to 424 assaults during the same period.

The Israeli occupation forces continue to raid the headquarters of the Palestinian security forces and fire on those headquarters. They also mount military check points in their vicinity where the number of provocations by the Israeli forces against the Palestinian security forces during the second half of 2009 totaled 97.

11.5 Settlement Activities and Settlers Assaults

Settlement activities in the Occupied Palestinian Territories continued, reaching 20 settlement activities during the second half of 2009. They included mounting military watch towers, building new housing units in the settlements and land scraping agricultural lands. Assaults by Israeli settlers against Palestinian citizens and their properties continued during the second half of 2009 to reach 357 attacks including the occupation of Palestinian citizens' houses, shooting and attacks. Three children and one adult citizen were run over by cars. The

settlers had also destroyed citizens' cars and their crops in addition to stealing and killing sheep from citizens' farms.

12. Palestinian Population in the World¹⁷

12.1 Population Census

The Palestinian population at the end of 2009 is estimated at 10.88 million. Their distribution consists of 36.7% in the Palestinian territories, 11.5% living behind the Green line, 29.8% in Jordan and 16.3% in the rest of the Arab countries, while the percentage of the Palestinian population in foreign countries reached 5.7%.

11.2 Palestinian Population in the Palestinian Territories

The population in the Palestinian Territories is estimated at about 4.0 million at the end of 2009, where 62.1% reside in the West Bank, and 37.9% in the Gaza Strip. On the other hand, the Palestinian population in the Jerusalem governorate amounted to 9.5% of the total population in the Palestinian Territories. Available data for 2009 indicate that the proportion of Palestinian refugees in the Palestinian territories is 45.0% of the total Palestinian population. 18.8% of them reside in the West Bank and 26.2% in the Gaza Strip, where the percentage of the refugees in the West Bank amounts to 30.2% of the total population and 69.2% of the total population in the Gaza Strip.

The crude birth rate in the Palestinian territories amounted to 32.7 births in 2009, with a drop from 42.7 births per 1000 of the population in the year 1997. This is attributed to the low fertility rate in the Palestinian territories. As for the regional level, there is a variation in the crude birth rate between the West Bank and the Gaza strip, where the crude birth rate in the West Bank declined from 41.2 births in 1997 to

¹⁷ The PCBS, press report: (PCBS President reviews the harvest of 2008, Israel crowns its siege of Gaza with aggression; the number of Palestinians reached 10.6 million, more than half living in the Diaspora), 31/12/2009.

30.1 births in 2009. In the Gaza Strip, crude birth rate declined from 45.4 births in 1997 to 36.9 births in 2009.

The crude mortality rate in the Palestinian territories was 4.3 deaths per 1000 of the population in 2009, less than the 1997 level of 4.9 deaths per 1000 of the population. On the regional level, a slight difference is noted in the raw mortality rates for the West Bank and the Gaza Strip, where the crude mortality rate dropped from 5.1 deaths in 1997 to 4.4 deaths in 2009 in the West Bank; while the crude mortality rate dropped from 4.7 deaths in 1997 to 4.1 in the year 2009 in the Gaza Strip.

12.3 Palestinians in Israel

The estimated number of Palestinians in Israel reached around 1.25 million at the end of 2009. The data available for the year 2007 on the Palestinians living in Israel show that they are a young population as the proportion of individuals aged 15 years or less is 40.6%, while those aged 60 or above is 3.2%.

The total fertility rate for the Palestinians in Israel was around 3.62 births per woman in the year 2007, a relatively high rate compared to general fertility rates in Israel. Data indicates that the average size of a Palestinian family was 5.0 individuals during 2007. The raw birth rate was about 27.3 births per 1000 of the population in 2007. Infant death rate in the same year was 7.2 for each 1000 infants alive, given that the ratio of men to women was 103.6 males versus 100 females. The illiteracy rates among the Palestinian population aged 15 and above amounted to 6.1%.

12.4 Palestinians in the Arab World

The total estimated Palestinian population in the Arab countries amounted to about 5 million at the end of 2009, more than two thirds live in Jordan. Data available on Palestinians living in Jordan illustrates that it is a young population, the proportion of individuals aged 15 or less amounting to 35.9%. The average size of the Palestinian family reached 5.1 individuals. The total

fertility rate for the Palestinian population living in Jordan was 3.3 births per woman.

Available data on the Palestinians living in Syria for the year 2007 show that the proportion of individuals aged 15 or less amounted to 33.1%. Data has also shown that the average size of the Palestinian family was 4.9 individuals. On the other hand, the total fertility rate for the Palestinians living in Syria reached in 2007, 3.64 births per woman and the crude birth rate amounted to 29.3 births for each 1000 of the population.

In Lebanon, the proportion of Palestinian individuals aged 15 or less amounted to 32.9% while the ratio of men to women was 98.4 males versus each 100 females during the year 2007. 2007 data indicates that 0.5% of families range between 6-7 individuals. On the other hand, total fertility rate reached 3.0 births per woman in 2007.

13. Israeli Assaults on the Health Sector¹⁸

The data issued by the Ministry of health points out the frequency of the assaults on the health sector by the occupying forces. These assaults include attacks on medical personnel, clinics and health centers in addition to assaults on ambulances impeding their movement as well as holding them. The Ministry of health recorded about 22 assaults during the first half of 2009 that affected the health sector in the Palestinian Territories.

13.1 Assaults on Ambulances

The number of direct assaults on Palestinian ambulances during the first half of the year 2009 was 3 assaults, all in the Gaza Strip governorates. In Jerusalem, an ambulance was searched and its entire apparatus was dismantled. The Israeli forces held and impeded two ambulances in Jerusalem

¹⁸ The Ministry of Health (2009). The Palestinian Statistical Health Report, the first half of 2009. Palestinian Health Information Center, Ministry of Health. Ramallah – Palestine.

villages, in addition to impeding and holding 3 other ambulances in various parts of the West Bank.

13.2 Assaults on Medical Personnel

The number of paramedic martyrs hit by Israeli bombing while they were in ambulances was 4 in the Gaza Strip in the first half of 2009. Two other paramedics were injured. In the West Bank, two paramedics were injured in the Hebron governorate after a direct assault on them by the occupation forces, in addition to injuring another in the Ramallah governorate as a result of being hit by a sound grenade. An ambulance driver was attacked in Jerusalem.

13.3 Assaults on Clinics and Health Centers

A clinic and a health care center in Gaza and the KhanYunis governorates were bombed during the first half of 2009.

13.4 Assaults on Public & Private Hospitals

Various assaults on Palestinian hospitals occurred including bombing, sieges and raids. During the first half of 2009 two hospitals in the Gaza Strip were directly bombed by the Israeli forces during their aggression against the Gaza Strip which began at the end of 2008 and continued in 2009. One of the hospitals in the old city of Hebron was besieged and another hospital in the Jerusalem area was raided by the Israeli Defense Army.

Economic Issues
Economic Growth (4)
Relation between Economic Growth and Foreign Trade

This is the fourth part of the series of economic issues that we started in the Monitor. This series focuses on 'economic growth'. We have studied in the first part 'what is economic growth, its definition and measurement'. The second part was allocated to 'sources of growth' where we found that growth happens either as a result of an increase in production factors (the physical capital and the human capital), or as a result of an increase in factors of production (which are products of technological progress, or an increase in the efficiency of productive institutions). The third part of the series (*Monitor 18*) focused on the relation between economic growth and income distribution, where we concluded that adopting a "pro-poor growth" strategy has many advantages. It encourages the accumulation of physical capital, motivates investment in the human capital and creates the appropriate environment for accelerating the process of technological progress and enhancing production efficiency. In this part, we will continue the search for the optimum environment that stimulates economic growth. In particular, we will focus on growth on the one hand and on trade openness and integration with the global market on the other.

Most studies confirm that there is a positive correlation between the degree of openness to global markets (foreign trade) and the growth rate in the GNP. A well known study of the World Bank (1987) divided the world into four groups: countries with high level of openness, countries with moderate level of openness, countries somehow closed and extremely closed countries. The study concluded that the average income growth rate was the highest in the first group during the period 1973-1985 while it was negative in the closed countries during the same period.¹⁹

Another study found that the average annual growth rate in open developing countries reached 4.49% while this rate did not exceed 0.69% in closed developing countries during the period 1960-1989.²⁰ Many other studies that applied theoretical models and various statistical methods at different periods of time, using different definitions of trade openness, came to the same conclusion which confirms the strong correlative relationship between the level of trade openness and the income growth rate.²¹

Nevertheless, the correlation between these two variables does not necessarily mean that there is a direct causal relation between trade openness and growth. This correlation may be a result of one or more of the following four probabilities: first, that growth is created or influenced by trade openness; second, that growth and openness are both affected by a third variable; third, that there is an inverse relation from growth to trade where growth promotes foreign trade; fourth, that the causal relationship is dual and two-way, where growth leads to increased trade and this in turn leads to growth. Briefly, this means that the correlative relationship does not necessarily indicate a direct causal relationship between variables. Therefore, the confirmation or negation of the causal relationship requires close examination into the potential impact of trade openness on growth and its sources, which we will do in the following paragraph. The last paragraph will be allocated to demonstrate the point of view of those schools which question the causal relationship between openness and growth.

The Impact of Foreign Trade on the Factors Determining Growth

Income or the GDP is subject to two types of influences. The first type leads to the rise or drop of the income level without affecting its growth rate or the rate of its sustained decline. The second type is the influence on the rate of increase and not only on the income level. In other words, the first influence occurs for one time while the second is sustained because it affects the rate of growth. Foreign trade may therefore influence growth through these two channels. This means that when trade leads to increased production, due to the utilization of the comparative advantages and the economies of scale, this in turn leads to a raise in income for one time. As soon as these advantages have been utilized the gains come to an end. These are called static advantages. But when foreign trade leads to raising the productivity of growth factors (due to technology transfer and competition), this raises the growth rate and leads to sustainable persistent increases in income. These are called the dynamic influences of

¹⁹ World Development Report 1987, Washington DC, World Bank, p. 83.

²⁰ Jeffrey D. Sachs and Andrew Warner (1995), "Economic Reform and the Process of Global Integration" Brookings Papers on Economic Activity, No.1, pp.350-36.

²¹ Hendrik Van den Berg(2001) Economic Growth and Development, New York: McGraw-Hill. P.327.

foreign trade. We will continue below the research into the channels through which trade influences growth and whether this impact is limited to the level of income or affects the rate of growth.

❖ **The Impact of Trade and Openness on Physical Capital**

Trade in itself has no direct impact on the physical capital. However, it is normal for countries that adopt a liberalization trade policy to liberalize the capital movement across borders as well and to encourage foreign direct investment (FDI). This means that the economy that is open to global markets is differentiated from closed economies in that its annual local savings do not impose a restriction on the size of annual investments, as it can finance its investment by borrowing from foreign capital. Also, the direct investments of foreign companies usually increase the capital available in the local economy.²² Various empirical studies did not always support this argument where several other studies revealed that most foreign direct investment (FDI) is between rich countries and only a very small part goes to developing countries.²³ Although the situation has somehow changed in the past ten years with increased flow of foreign capital to developing countries, but not to the extent which effectively impacts the economic growth.

❖ **The Impact of Foreign Trade on Human Capital**

There is a significant impact for the foreign trade and openness in general on the formation of human capital. Reading foreign periodicals and books, using the internet and being exposed to other schemes of work and thinking are all types of exchange and trade with the outside world. What citizens learn from these external sources adds to their culture and expertise. Moreover, the foreign companies that practice an economic activity in the local market usually train local labor in modern production and marketing methods and organize training courses for local workers, this all adds to the formation of local human capital.

As we have seen in part three of this series, the increase in productivity emanates from two sources: technological progress and production effectiveness. In the following, we will address the impact of trade on each of these components of productivity.

(a) **The Impact of Foreign Trade on Technological Progress**

Foreign trade leads to technological progress in two ways. The first has to do with the transfer of new technology from abroad to a given country. The second is about the possibility of generating modern technology in the country itself.

As for the first way, the country that has liberalized trade can import modern technology easily and more effectively than a closed country. The open country imports modern technology together with ‘capital commodity’ imports, i.e. machinery, equipment and apparatus. The foreign direct investment builds new factories that operate according to new technological methods, in addition to the communication and interaction between various countries that leads to the so called transfer of ‘soft technology’, such as modern management techniques and modern marketing methods. In order to know the extent of the impact of the ‘transfer of technology’ on the technological progress in rich countries, a study measured the proportion of technological progress attributed to ideas that were originated outside in the OECD countries. The study concluded that most technological progress in all OECD countries, with the exception of the United States, has been through the transfer of ideas that were born outside.²⁴ For instance, the study found that 97% of the technological progress in Canada has been through ideas of external origin. In Japan, this proportion is 73% while in the United States, 18% only of the technological progress has been achieved by ideas from abroad.

The other way in which foreign trade influences technological progress has to do with the incentives to spend on research in local economic enterprises. The main incentive for spending on research is the profits expected from the creation of a new technology or a new commodity.

²² See Feldstein, Martin, and Charls Horioka (1980). “Domestic Saving and International Capital Flows”. *Economic Journal* 90 (June): 314-329. And Obstfeld, Maurice & Alan M. Taylor (2002) “Globalization and Capital Markets” *NBER Working Paper* 8846.

²³ See Maddison, Angus. (2001) *The World Economy: A Millennial Perspective* . Paris: Development Center of the Organization for Economic Cooperation and Development.

²⁴ See Eaton, Jonathan, and Samuel Kortum (1996) “Trade in Ideas: Patenting and Productivity in the OECD” *Journal of International Economics* 40 (May): 251-278.

Obviously, these expectations are higher when the new invention or commodity stands an open chance for exportation and existence into markets larger than the local market.

(b) **The Impact of Foreign Trade on production effectiveness**

The most important impact of foreign Trade on productivity is through its impact on effectiveness. Trade liberalization means that protection is removed from local enterprises exposing them to competition with foreign enterprises. This is known as the ‘bracing effect’ where local enterprises face a difficult choice, either improving productivity or bankruptcy. Improving productivity is done through the elimination of the distortions that have accumulated as a result of protection. What happened in Canada is a classical example of the improvement of productivity after the removal of protection following the signing of the free trade agreement with the United States in 1989. The productivity of the protected companies increased (after lifting the protection) three fold compared to the productivity of those that were unprotected. Another example is from India where the industry of machinery was protected by a 100% tariffs. When the Indian government lifted this protection through a large reduction in customs, Taiwanese companies were rapidly able to enter the market and obtain one third of the Indian machinery industry market. This forced the Indian companies to take the difficult and necessary procedures to improve their productivity in such a way that they regained their position within 10 years in the local market and started exporting. There are also many other example in this regard.²⁵

Skepticism in the ability of foreign trade to raise the economic growth rate

In economic literature, there are studies that shed doubts on the ability of foreign trade to accelerate economic growth and some even say that the relationship between foreign trade and growth may be negative. There are two types of these studies, the first type relies on the assumption that the studies that found a strong correlative relationship between the degree of an economies openness and the economic growth rate had reached such a conclusion by ignoring other significant factors. The countries that adopted trade liberalization had done so within a comprehensive reform policy system that included financial, monetary and judicial systems reform as well as confirming property rights and enhancing competition. When the impact of these reforms is added to trade liberalization, it is realized that trade liberalization by itself is not that a significant a factor as those studies which focused on its impact on growth have claimed, neglecting the other factors.²⁶

It is worth noting that advocates of this view do not deny the role of foreign trade as explained above, but they warn of the mistaken belief that the abolition of customs and non-tariff restrictions are capable of automatically accelerating growth. They also highlight evidence to prove that trade liberalization mostly comes as a result rather than a preface of growth, that starts by the promotion of investment in physical and human capital and by comprehensive reform in the political and economic fields.

The second type of studies assert some theoretical considerations that find a benefit in protecting certain commodities from foreign competition even for a limited period of time, and find that it is wrong for the poor developing countries to liberalize trade totally and at once. There are three theoretical arguments in this area:

(a) Strategic Argument for Trade Protection

This argument is based on two premises. The first is that full foreign trade liberalization leads to the specialization of each country in the manufacturing of commodities that they have comparable advantages in their production and to import the commodities that other countries have a comparative advantage in. However, this may restrict poor countries to the production of commodities of simple technology, imprisoning them in a low technological environment and negatively affecting their growth in the long run.

²⁵ See David N Weil: *Economic Growth* (2005) New York: Pearson. Chapter 11.

²⁶ See Rodriguez, f and Rodrik, D (2000), “Trade Policy and Economic Growth: A Skeptic Guide to Gross National Data”, *NBER Macroeconomics Annual*.

(b) Infant-Industry Argument

This argument relies on the fact that any infant industry needs a specified period of time in order to achieve competitive advantages. Thus when protection is removed, this industry will not be able to stand facing foreign competition. Therefore, it is necessary to provide the infant industry with this protection at its outset for a limited time until it obtains a comparative advantage, enabling it to compete with foreign powerful industries.

(c) The Structuralist Argument for Import-Substitution

This argument claims that when developing countries adopt trade liberalization, they choose to maintain the economic pattern established during the colonial era, represented in importing industrial commodities and exporting primary and agricultural commodities. However growth and progress will only be achieved through changing this pattern and establishing an industrial base. This requires protection from the competition of foreign industries for a certain period of time.

There were many supporters of these arguments in the last century, but the practical experiences and the weak theoretical foundation of some of these arguments, besides the misuse of tariff protection which lasted for long periods of time and was applied for the self-interests of certain parties, had stripped it of much of its credibility in the last decades. Nevertheless, it is necessary to emphasize that the random and rushing openness is accompanied with an economic high cost. Also, that some of the ‘pessimists’ schools ideas on the role of foreign trade are still valid (the infant industries and the strategic dimensions), and that the comparative advantages are not natural traits of countries but can be generated and nurtured through the appropriate economic policies.²⁷

On the other hand, we should not ignore that rich countries still apply selective trade protection (on agricultural products to be specific) and that this is very costly for poor countries. A study has revealed that poor countries loose about \$100 billion annually as a result of trade protection procedures imposed by rich countries.²⁸

²⁷ See Ha- Joon (2002). *Kicking Away the ladder*. Cambridge U.P.

²⁸ See Dollar, David, and Art Kaary (2002). “Growth is Good for the Poor” *Journal of Economic Growth*, 7 (September): 195-225.