



Palestine Economic Policy Research Institute (MAS)

Background Paper

Roundtable (2)

**Termination of US Aid to Palestine:
Economic and Social Repercussions and Ways Forward**

February 2019

This background paper provides a detailed review of aid in its historical and political context from the Government of the United States (US) to the Palestinian people in the West Bank and the Gaza Strip, which completely ceased in 2019. The paper traces the flow of aid from 2001 and analyses its trends, sectoral components and mechanisms of delivery, in order to accurately identify the potential consequences of the cessation of aid on vital programs and sectors still requiring continued support. It then examines some available financial policy options that could help the Palestinian people combat these US and other financial sanctions without jeopardizing social subsidies to the poorest and most vulnerable groups, and without having to defer the public investment program needed to build a more self-reliant economy.

1. Historical and political background of US aid to the Palestinian people

Since the 1948 Nakba and the ensuing Palestinian refugee crisis, the US has been the largest donor to the Palestinian people and a major political player in the region. American assistance to Palestine began with the creation of the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) in 1949. UNRWA is the first international humanitarian organization established by the international community as a recognition of its responsibility for the Nakba that befell the Palestinian people who were displaced in the wake of the occupation of 80% of Palestine and the establishment of the State of Israel. In addition to US funding for UNRWA, which has flowed for the past 70 years, the US Agency for International Development (USAID) has funded humanitarian and social assistance programs in the occupied Palestinian territory since the 1980s through US non-governmental organizations. Following the Oslo Accords and Washington Agreements, the USAID started implementing programs in various sectors in the West Bank and the Gaza Strip. As of the second intifada, the United States also started providing direct financial assistance to the budget of the Palestinian National Authority (PNA). In the years following the Palestinian internal divide of 2007, US aid broadened in scope and size to include various areas of governance, nonlethal security, emergency relief, social services, economic development and infrastructure.

This consistent policy of providing US aid to the Palestinian people (however much it varied over 12 Republican and Democrat administrations) was dealt a strong – possibly fatal - blow by Donald Trump's decision to cease as of 2018-2019 all US aid to the Palestinian people (contributions to UNRWA, USAID programs and other bilateral economic assistance). It is well-known that donor countries' assistance to the Palestinian people, including that by the United States, has always been linked to the policies of these donors towards the Palestine question, fluctuating in size, form, channel and goals according to their changing political positions and their global and regional developmental agendas, especially in the 25 years that followed the Oslo Accords. Social and economic consequences of such move aside, Trump's aid cutoff is unprecedented in the history of the US-Palestinian relationship and it constitutes a critical escalation of political pressure and a hostile attitude not only towards the Palestinian Liberation Organization (PLO) and the PNA, but also towards the Palestinian people and their politics. Ilana Feldman (2018) observes that "the assault on UNRWA is a full spectrum assault on Palestinian politics."

No matter the justifications that this administration offered for its extreme decision, they did attempt to deny that the aid cutoff is tantamount to collective punishment of the Palestinian people as a whole, or a US political and financial reaction to PLO's refusal to submit to the Trump administration's positions towards the Palestinian question, on Jerusalem and Palestinian refugees, not to mention its complete alignment with Israel's settlement policies (Congressional Research Service, 2018). The decision to cease support for the West Bank and the Gaza Strip is by all accounts a strategic reversal of the decades-long US view of its international responsibilities and its role as a sponsor of the Middle East peace process in particular. The new US position put an end to its constant attempts to appear as a "honest broker", which indeed never was committed to promoting Palestinian welfare and good governance as it was to defending the ambitions of its biggest security, political and economic ally in the region, Israel. This drove 34 US Senators to send a letter to Trump saying: "We are deeply concerned that your strategy of attempting to force the Palestinian Authority to the negotiating table

by withholding humanitarian assistance from women and children is misguided and destined to backfire" (Congressional Research Service, 2018).

It is true that many US international foreign (and domestic) policies have been overturned since Trump came to power along with a team hitherto unknown in US foreign policy, and that the Palestinian issue, like others, was subject to Trump's controversial method of governance– alternating between improvisation and chauvinism. Apart from being a cowardly political blow, this foreign policy has particularly critical humanitarian and social implications in the Palestinian case. Regardless, it seems that we are facing a fundamental change that is unlikely to change under this Administration (in the next two to six years), not to mention the difficulty of predicting future US policy even after its departure.

In the following sections, we look at the development of US aid to Palestine, focusing on the 2001-2018 period– which witnessed three different administrations (Bush Jr., Obama and Trump)– and its sectoral distribution, some of which was vital for large segments of the Palestinian people, such as poverty, food security, healthcare and education services. The paper also looks at the consequences of the aid cutoff on some major sectors that require an urgent international and Palestinian funding response to spare the poor and refugees paying the price of this harsh US policy.

2. Channels of US aid to Palestine, 2001-2018

As stated above, US assistance previously focused on three main areas: support to UNRWA through multilateral funding mechanisms / programs, bilateral humanitarian and development aid through USAID, and foreign and security policy programs bilateral assistance delivered through government agencies, especially the Department of State.

2.1 Multilateral Assistance (UNRWA): As the largest donor to UNRWA, the United States had contributed a total of \$ 6.25 billion since 1950. The contribution reached a peak of \$ 400 million in 2014, declined to \$ 360 million in 2016 and 2017 and wined down to only \$ 65 million in 2018 before it was completely stopped in 2019 (Congressional Research Service, 2018). That US funding was allocated as a contribution to UNRWA programs that educate 525,000 Palestinian (refugee) students, provide food assistance to around one million refugees in the Gaza Strip and contribute to public health services for the refugee population in Palestine, Jordan, Syria and Lebanon. The final US decision to cease funding to UNRWA after 69 years of support came in August 2018 on the pretext that the United States was no longer willing to shoulder the disproportionate share of the burden of UNRWA's operations because, the administration reasoned, "the fundamental business model and fiscal practices that have marked UNRWA for years –tied to UNRWA's endlessly and exponentially expanding community of entitled beneficiaries –is simply unsustainable and has been in crisis mode for many years" (ibid). What is, however, not explicit in the official US statements is the conviction that the very existence of UNRWA reinforces the endurance of the question of refugees and their right to return to their homes at the forefront of contentious issues, which have frustrated the administration's attempts to impose its agenda known as "the deal of the century" (ibid; Feldman, 2018). The continued US support for other refugee programs in the region is further proof that the only US goal in cutting UNRWA funding is its complicity with Israeli schemes to dissolve the cause of the Palestinian refugees.

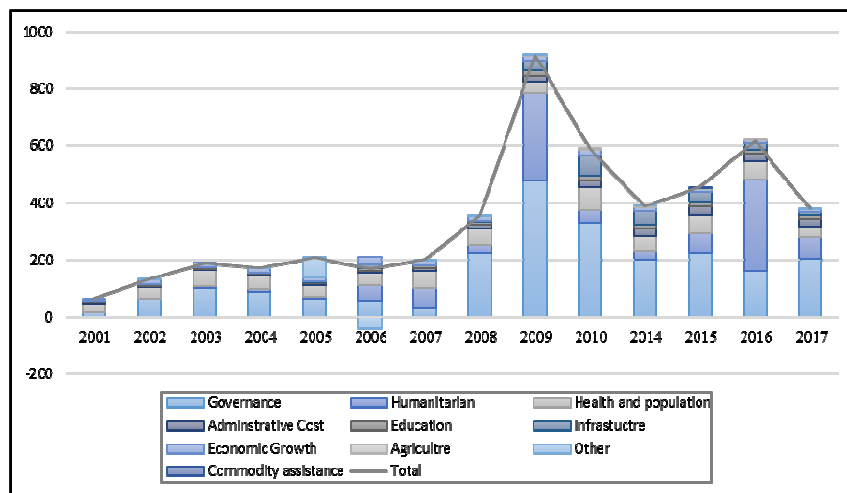
2.2 Bilateral (direct) assistance: According to USAID data (2019), the United States provided via its different channels a total of \$ 6.9 billion in aid to the Palestinian people in the occupied territory between 2001 and 2018 (an average annual rate of \$ 385 million). Prior to 2001, the aid had never exceeded \$ 100 million annually. Since then, however, it grew, reaching \$ 200 million in 2007 in response to the humanitarian crisis in the aftermath of the second intifada. By 2009, it had reached an all-time high of \$ 890 million before it declined slightly to \$ 830 million by 2011 in support of the budget of the PNA and its efforts toward building state institutions during that period. Of course, fluctuations in aid were not only linked to the volatile political and security events (the intifada, the internal divide, the reform stage, etc.), but also to the PNA's limited absorptive capacity and the US-

Palestinian bilateral agreements, as well to selectivity and disparity between humanitarian, social, economic and security priorities.

Apart from these determinants of US aid, each administration, it appears, had more or less sympathy, or hostility, toward the Palestinian people; and change in the scale of financial assistance reflected differences in the approaches of US administrations to the Palestine question. In the first three years of Obama's term, US aid reached \$ 2.3 billion, and throughout his two terms, assistance to the Palestinian people totaled \$ 4.9 billion or 71 % of the US total aid since 2001, while aid during Bush's 8-years in office constituted 21 percent of the total aid in the period. In stark contrast, the overall spending during Trump's first two years was hardly \$ 522 million, the majority of which was planned prior to his assumption of power.

A range of US government agencies have administered the process of planning and spending of bilateral aid provided under the Economic Support Fund account, especially via USAID, the Department of State, the Department of Defense, the Department of Agriculture, the Department of Treasury and some other agencies. Part of the assistance to the Palestinian people was provided through international or regional security and political programs such as the Nonproliferation, Anti-terrorism, Demining and Related Programs (NADR)" and International Narcotics Control and Law Enforcement (INCLE). USAID administered the largest share of US aid (more than 90% between 2001 and 2006). As of 2007, nevertheless, other agencies began funding the PNA, and implementing programs in institutional development, rule of law and establishing security. USAID's contribution since then remained steady at 60-80% in most years, yet it peaked in 2009-2013, with a total of \$ 2.3 billion spent during that five-year period. The only year in which USAID's share of total US assistance was less than half of total US aid was 2016, when funding for USAID programs was \$ 284 million (46% of the total). Since US agencies (mainly Department of State and Department of Agriculture) started spending significantly on particular programs in Palestine (\$ 70 million in 2007), allocations for these programs have rapidly increased to \$ 360 million in 2009 and \$ 332 million in the last year of Obama's presidency (see Figure 1 below).

Figure 1: Direct US aid to the West Bank and Gaza Strip, By major sector, 2001-2017 (\$ million)



Source: USAID Database (accessed at <https://explorer.usaid.gov/aid-dashboard.html>), 2019

3. Strategic sectoral assistance and the consequences of cutoff on Palestinian economic and social conditions

With such developments in US aid (particularly the significant rise in the post-2008 period and the gradual decline in the subsequent years, leading to a complete halt in 2018), more than half of the aid

remained concentrated in the governance sector (with its wide-range of subsectors), reflecting the donor's priorities and response to changing Palestinian conditions (relief, reform, development, etc.). The share of governance in 2009 (the year in which aid reached its peak) and 2017 (the last year of US aid before cutoff) accounted for 52% and 54%, respectively, although total aid in 2017 was only one-third of its 2009 level, reflecting a US relatively constant attitude toward this particular sector. main areas: government and civil society (\$ 116 million and \$ three in allocated Governance aid is ¹ 84 million in 2009 and 2017, respectively), conflict, peace and security (\$ 335,000 and \$ 17 million) and a large share in social services. Indeed, the largest amounts under the governance program were earmarked for social welfare services for the poor – with allocations declining from \$ 362 million in 2009 to \$ 104 million (or 28 percent of total aid) in 2017. Out of the 11 programs under the "government and civil society" category (which covers legal, civil, informational and institutional areas of governance), the largest share was for legal and judicial reform (\$ 116 million and \$ 83 million in 2009 and 2017, respectively).

The most significant change in aid to other sectors was the shift away from the humanitarian priority characteristic of the pre-2010 period. In 2009, emergency relief (in-kind assistance and food) amounted to \$ 305 million (33% of total aid). The figure dropped to \$ 74 million (or 20% of total aid) by 2017. Humanitarian relief programs were, thus, the second largest overall beneficiary (with an average 24%) of US assistance since 2001.

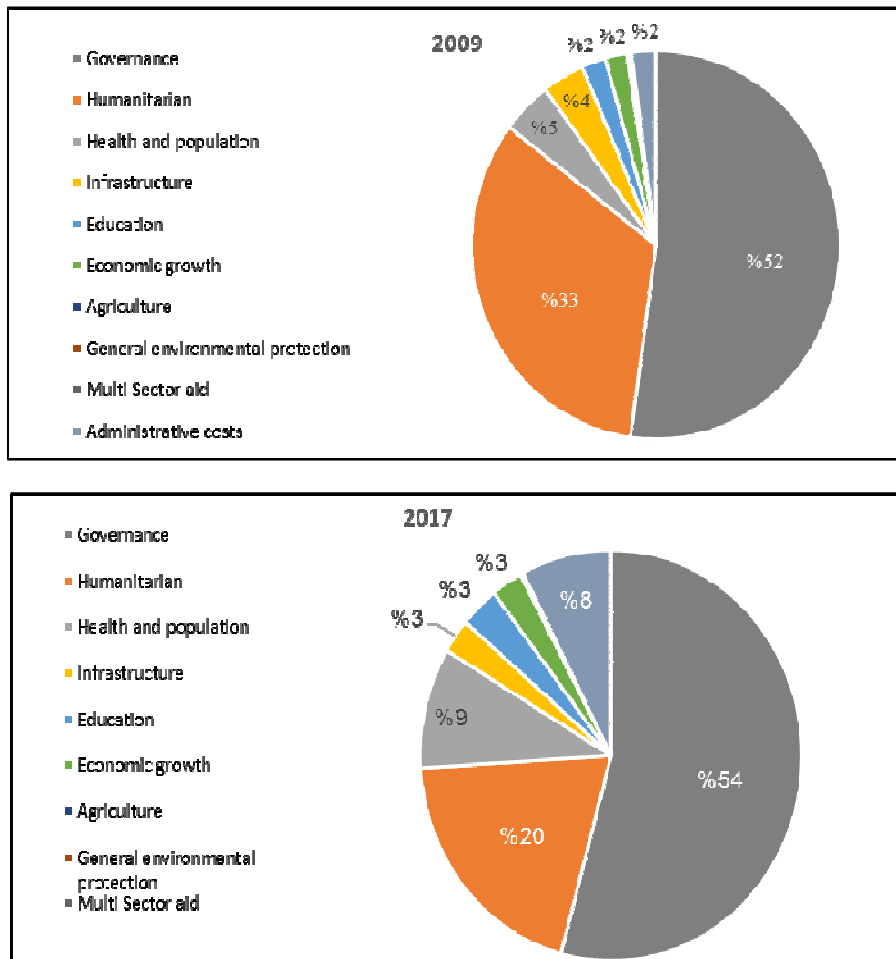
This decline in the value of humanitarian assistance mirrored a similar decrease between 2009 and 2017 in aid to infrastructure (especially transport / road and storage), education (primary education, higher education, teacher training), economic development (business services, trade policy, and the development of the industrial sector, especially micro-enterprises), falling by 70%, 37% and 44%, respectively. In 2017, the combined share of these sectors (only \$32 million) was less than 9% of US aid. Despite the overall decline in aid to the health and population sector (including the provision of safe drinking water, basic health care and health management) from \$ 40 million to \$ 35 million between 2009 and 2017, its share of total US assistance increased from 4.4% to 9.5% between those two years.

In what seems like a common approach by all donor countries, the agriculture sector received little US aid (\$ 2.3 million in 2009 and a meager \$ 386,000 in 2017, or 0.1% of total aid). Over a period of 18 years, US aid to Palestinian agriculture totaled \$ 29 million, a miserable 0.4% of total US aid since 2001.

Finally, as is often with all donor countries, the financial costs of managing the planning and spending US assistance are counted as part of that assistance to Palestine. Such costs increased from \$ 19 million in 2009 to \$ 29 million in 2017. While aid fell dramatically during that period, the financial costs ballooned from 2% to 8% of total aid. It is unclear how the US administration was able to pump nearly \$ 1 billion in aid in 2009 at a much lower administrative cost than that of managing one-third of the amount in 2017. This may be due to more scrutiny of aid expenditure that has of late been employed for political or operational reasons, as well as for the imperative of economies of scale when providing humanitarian and social assistance and substantial budget support in 2009 compared with 2017.

¹ Rationale for choosing these two years: 2009 was a year of humanitarian crisis, while 2017 was an ordinary year.

Figure 2: Sectoral allocation of US aid– 2009 and 2017



Source: USAID Database (accessed at <https://explorer.usaid.gov/aid-dashboard.html>), 2019

The sectoral allocation of aid in 2009 vs. 2017 (as shown in Figure 2 above) reveals two main constants: a commitment to building PNA institutions and a recognition of the magnitude of the humanitarian and social suffering of the Palestinians. This comes within a US liberal economic philosophy that development is based above all on institutional reform (good governance) and the welfare of the poorest (social safety nets), while decisions regarding economic activity are solely guided by the markets, with limited governmental interventions to unleash market forces. Although this development orthodoxy has become outdated and proved ineffective in bringing radical development transformations in Palestine and in many other countries, US commitment in the Palestinian case to the set of policy prescriptions advocated by the "Washington Consensus" (which governs the advice and funding of international financial institutions and the US Treasury based in Washington D.C.) comes as no surprise. Apart from the economic ideology underlying that philosophy, the structure of US aid to the Palestinian people reflects the American ideation of the desired political form of a Palestinian state, which the United States had (at least until Trump's administration) stressed the necessity of its establishment.

4. The major sectors and groups affected by the cessation of aid and the alternatives that can compensate for lost aid or mitigate its consequences

In addition to the established economic doctrine underlying the programs the US government implemented in aid to the Palestinian people (the insufficient support for productive sectors, the exaggerated focus on institutional reform, and the considerable administrative costs), US assistance has come under more severe criticism. Some believe that channeling part of the aid to projects that make the Palestinians adapt and acquiesce to a *de facto* occupation (e.g., through road network projects linking some Palestinian towns through colonial settlements or through bypass, winding roads around those settlements on the pretext of improving the "fabric of life" of the Palestinians) only perpetuates, rather than changes, the current conditions in the Palestinian occupied territories (Jabary-Salamanca, 2016). Others see the American decision to cease aid as an unintended gift to the Palestinians because it frees them from dealing with Trump's hostile administration and enhances Palestinian political and financial independence, assuming that alternatives do exist or that the aid can be readily dispensed with as it was never meant to serve Palestinian national interests (Tartir and Wildman, 2019).

It should be made clear, however, that the paper does not aim to assess the effectiveness or probity of US aid to the Palestinians; rather, it examines its components so as to make it easier for the Palestinian economic decision-makers to identify the sectors that may be troubled by the cessation of US aid and the previously US-supported programs that can be abandoned without a negative impact. It should be stressed that this aid is not a handout, a humanitarian gesture, a signal of the generosity of the American people or even an American recognition of the rights of the Palestinians. The true reason why the United States continued to financially help the Palestinian people for 70 years is that aid for the Palestinians is understood as an indispensable entitlement and political *sine qua non*, and it should remain so until a just settlement of the Palestinian question is reached. Thus, receiving aid from any side shouldn't be understood as compliance with international political interests / agendas, nor should it mean that the basic rights of the 5 million Palestinian refugees can be protected or that the PNA can be maintained under the occupation without international financial assistance, no matter how often it fluctuates. It is that which amplifies the scale of the harm inflicted by the US administration when it decided to cease aid to Palestine, let alone its other unjust decisions, such as recognizing Jerusalem as the capital of the State of Israel. The imperative to face the aid cutoff decision entails not only finding alternatives, but also not allowing any side to infringe upon Palestinian basic living rights through imposing such financial sanctions.

Looking at the framework of US aid in 2017, the vital and less important sectors can be identified as follows:

4.1 UNRWA Financing: One of the most appalling aspects of the US decision is ending funding of UNRWA. At stake is UNRWA's financial sustainability and its ability to continue delivering health and education services to the refugee population. In addition, the cessation of aid has implications regarding the US position towards the issue of the Palestinian refugees. Some analysts say that stopping funding of UNRWA echoes well with the approach Trump's administration has taken toward the question of Jerusalem ("taking the issue off the negotiating table") in a phased abolition of the so-called "permanent status issues" that were deferred to permanent status negotiations under the Oslo Accords. To date, UNRWA seems to have been able to replace American aid with increased funding from European and Arab donors (\$ 425 million in pledges to cover its 2019 deficit). With some countries demanding that UNRWA adopt austerity measures in spending on services to refugees, many observers warn of the dire social consequences of further austerity in the Agency's already tight services in Palestine and the refugee hosting countries. UNRWA's financial sustainability, under such conditions, does not seem to be guaranteed, and therefore the United States should not be absolved of its historical political responsibilities towards Palestinian refugees, no matter the changes in its policies towards the Palestine question.

4.2 Bilateral vital assistance that should be urgently substituted: “Vital” funding may be considered that which cannot be suspended as it is directly related to services that ensure a decent life for Palestinian citizens as well as subsistence for the poorest or vulnerable groups. Table 1 below suggests priority programs which the government will have to finance whether using its own resources or through alternative international donors (at least \$ 250 million). Those affected by the US aid cutoff are beneficiaries who receive cash and food subsidies provided by the Palestinian government and its international partners, as well as beneficiaries of other programs (e.g. from building schools and medical assistance such as that provided to cancer patients). One look at the figures for these beneficiaries can reveal the prejudicial socioeconomic consequences of a new American policy that fights Palestine by assaulting its poorest segments. If funding of these vital areas stops, development and social welfare will suffer significantly. Obviously, failing to secure alternative sources for such vital sectors (particularly social development and humanitarian relief) could put an unbearable burden on disadvantaged Palestinian social strata.

Table 1: US Aid to Vital Economic and Social Sectors, 2009 vs. 2017 (million dollars)

	2009	2017
Social Welfare Services	362,200,572	103,743,830
Humanitarian relief	282,909,622	67,266,100
Food assistance	21,826,800	7,039,496
Providing water and sanitation	24,761,730	30,068,673
Primary health care	4,888,843	5,718,534
Travel and transportation	34,218,065	8,980,813
Education	19,592,159	12,341,803
Economic development	17,785,352	9,892,303
Agriculture	2,352,603	386,976
Total	770 million	245 million

Source: USAID Database (accessed at <https://explorer.usaid.gov/aid-dashboard.html>), 2019

4.3. Less important sectors (where US aid can be dispensed with or where the performance of the beneficiary sector does not hinge on such aid): Identifying such a typology aid is ultimately subject to discretion informed by different perceptions regarding how important/unimportant an item of expenditure might be. In all cases, however, the PNA should be able to manage the governance sectors that used to receive US support without needing to identify urgent alternative sources of funding, or around \$ 150 million of US annual support to various programs under the rubrics of governance, "peace-building", security and administrative costs.

4.4 Outlook of future US aid to the Palestinians: After the Palestinian decision in January 2019 not to receive the last remaining component of US aid (about \$ 60 million for security programs), it appears that the only thread that the US administration may keep with the Palestinian people is through a congressional bill that would establish a Palestinian Partnership Fund (with an annual budget of \$ 150 million). This is intended to facilitate and finance joint economic, research and investment ventures "between Palestinian entrepreneurs and companies in the United States and Israel."² The bill stipulates that "the fund's administrators would be precluded from discriminating against any community or entity in Israel, the West Bank, or Gaza" —presumably including Israeli settlements in the West Bank—“due to its geographic location" (Congressional Research Service, 2018). Perhaps more than any of the hostile American policies against the Palestinians since Trump assumed office, this project reflects the content and goals of the "Deal of the Century" and the depths

² [https://fortenberry.house.gov/sites/fortenberry.house.gov/files/FORTEN_049_xml%20\(002\).pdf](https://fortenberry.house.gov/sites/fortenberry.house.gov/files/FORTEN_049_xml%20(002).pdf)

to which US policies have fallen, to a level that erases the independent Palestinian entity and reduces it to a mere commercial partner of US and Israeli capital.

5. Conclusion

Therefore, under the best economic and political conditions, it might be possible to secure the \$ 250 million lost through US cessation of aid to vital sectors. However, if this American financial assault on Palestine's poor is accompanied by an escalation in financial sanctions that the occupation authorities threaten to impose on the Palestinian clearance revenues, which Israel is supposed to transfer in full and unconditionally (in what is effectively two fronts in one financial war), then the Palestinian financial and economic outlook in 2019 will be nothing if not alarming. Past episodes in 2006-2007 and 2011-2012 in the face of such international and Israeli financial sanctions have taught us that the banking system and the Palestinian treasury can live with such conditions for 3-12 months, as a MAS study suggested:

Depending on their duration, the impact of clearance revenues suspensions on the Palestinian banking system has been transmitted in past episodes through more PNA borrowing, the interruption of loan payments by PNA employees and private sector suppliers, and increased credit risk due to deteriorating economic conditions. So far, clearance revenues suspensions have not caused major disruptions to the banking system. Cooperative arrangements between the Palestine Monetary Authority (PMA), the PNA Treasury, and the banking system have been successful in past episodes in averting financial crisis (Hamed, 2017).

Another study by MAS– which looked into international experiences in financing the government's activities by prioritizing investment expenditures for the development of strategic sectors– reached the conclusion that it is possible for the Palestinian authorities to sustain more public deficit if emergency circumstances or development strategy require so:

Therefore, the PNA should first intensify its efforts to obtain funds from external donors, and eventually widen the scope of international partnerships (e.g. with a focus on Asia). The use of these grants should be embedded in a broader development strategy, so that donors would be reassured that the funds are directly invested in infrastructure and productive activities (not consumption!). Secondly, any legal restrictions on government debt accumulation should be avoided. Such a stance poses an entirely arbitrary limit to government finance, whilst disregarding saving and investment positions of other sectors. As long as a debt limit is not imposed, the government could take on extra credit with the PMA, where some room for maneuver appears to exist. The PMA, in turn, could enhance its capacities through a closer cooperation with the BoI, which should – at least – include the establishment of a credit facility to ease access to NIS reserves (Flassbeck et al, 2019).

In concluding, we pose a set of questions for consideration in discussing the interventions that can be deployed to survive the expected financial shock in the wake of US aid cessation (and any potential Israeli financial sanctions) and to secure full funding for the threatened PNA's social and investment programs:

1. What are the prospects for intensifying and diversifying efforts to obtain as much as possible of international grants (or loans) to finance public investment in infrastructure and productive economy?
2. What are the possible austerity measures in current spending? How tolerable they are, especially with regard to the operational budgets of the ministries? Should the PNA opt for delaying the pay of a certain portion of public employees' salaries (according to the salary range), encouraging early pensioning, or freezing new employment?
3. Can the tax compliance for existing taxpayers– or other measures– be raised to increase tax revenues without having recourse now to the tougher, more perilous expansion of the tax base?
4. Is the PNA prepared to deploy an investment and commercial program that stimulates the local economy and increases tax revenues from more domestic production?

5. Are there prospects for changes in trade policy that would reduce overdependence on clearance revenues to finance government activities?
6. What are the potentials that international programs affected by US aid cessation be compensated without cutting subsidies to the poor?
7. How can the State of Palestine legally and diplomatically object before international organizations to the US aid cutoff to UNRWA, on the grounds that it is an agency mandated with taking on an international legal commitment with which all UN member states must comply?

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