

The Palestinian Strategic Report 2006



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Chapter Nine

*The Economic Conditions in the West
Bank and Gaza Strip*

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The Economic Conditions in the West Bank and Gaza Strip

Introduction

Since their occupation of the WB and GS, the Israeli occupiers have persistently and consistently strove to completely annex the economy of these two regions to the Israeli economy. Hence this economy has become weak, uncompetitive, sluggish and submissive. It focuses on serving the Israeli economy in all aspects and by all means.

The occupation policies and activities caused defects and imbalance in the economic infrastructure of the Palestinian regions. The Israeli occupation authorities issued many military decrees and directives that aimed at usurping as much as possible of the Palestinian lands and economic assets. They, moreover, geared the Palestinian economic and social activities to be under the grip of the Israeli economy, and to sustain the occupied regions as an exclusive market to the Israeli goods and products.

The Palestinian economy had also suffered from the numerous policies measures that it was exposed to during the long years of the occupation in so far as opening up the Palestinian market to its Israeli counterpart. This had negative impact on the volume of investment and production of the Palestinian economy.

Indeed, the Israeli occupation succeeded in attaining its objectives. Admittedly a measure of increase in the standard of living of the Palestinian citizens took place, but this had partly resulted from annexing the Palestinian economy to its Israeli counterpart and not from a real development of the Palestinian economic sector.

The 1994 economic protocol, known as the Paris Protocol, which had been concluded after Oslo Agreement of 1993, had fixed and regularized the nature of the relations between the Palestinian and Israeli economies, and, to some extent, with the economies of Arab and other countries. In fact, the Paris Protocol had not changed the essence of the economic structure that had been imposed by the occupation, but only its form. For Israel continued its control of the passages, and

hence the entry and exist of the imports and exports of goods and raw materials. Moreover, the financial arrangements that resulted from the Paris Protocol enabled Israel to control the financial sources of the PA, particularly the right to collect its taxes and dues in a direct matter. Additionally, Israel had in many cases whimsically, and for retaliatory reasons, closed the various passages, which were, in fact, used as a means of political and economic pressure on the PA. This had, no doubt, substantially harmed the Palestinian economy.

By virtue of the Paris Protocol, the economic status of the PA is dependent on two variables. First, its relations with Israel, particularly with regard to the taxes that it collects on behalf of the PA, which constitutes 60% of the latter's overall taxes. Second, the relationship of the PA with the Western and Arab donor states, who funded many projects and the infrastructure, in addition to their role in supporting the general budget of the PA.

Following Hamas' overwhelming victory in the legislative elections and its formation of the Palestinian government, the economy of the WB and GS suffered during the year 2006 from an unprecedented and total siege by Israel and other countries, which was the tightest and most brutal of all blockades since the Israeli occupation in 1967. The blockade was used as a means of collective punishment to all the Palestinians of the interior, and had catastrophic repercussions on their economy, which lost 1/5 of the Gross Domestic Product (GDP) achieved in the year 2005. Hence, the Gross National Income (GNI) per capita was slashed, the rate of unemployment and poverty accelerated and economic stagnation reached unprecedented levels.

Even before the legislative elections and Hamas' assumption of power in 2006, the Palestinian economy in the WB and GS had experienced difficulties that were aggravated by *al-Aqsa Intifadah* of 2000. For Israel, had adopted the policy of prolonged blockade, separation of districts from each other, programmed destruction of institutions and economic installations, denial of work for the Palestinians inside Israel, procrastination in payment of the taxes and dues collected on behalf of the PA, continuation of building the Separation Wall which closed extensive areas in the WB, and the imposition of permanent barriers that restricted the movements of the Palestinians and their ability to fully exploit their lands. Some economists estimate the direct and indirect losses of the Palestinian economy since *al-Aqsa Intifadah* by about \$15 billion.

The economic crisis in the Palestinian territories reflects the extensive fragility of the Palestinian economy and its overwhelming dependence on foreign aids, particularly for funding the budget of the PA and other projects that are crucial for improving the living standard of the internal Palestinians.

It is worth mentioning at this juncture, the difficulty of having detailed data on the economic indicators for the year 2006, because of the then internal complexity within the Palestinian territories, and the marked irregularity in the functioning of the institutions of the PA. Nonetheless, the preliminary data and statistics that we have, indicate a regression in most of these indicators.

First: National Accounts

The preliminary estimates at constant prices issued by the PCBS for the year 2006 indicate a continuation of the dwindling in the GDP during the last quarter of the year, i.e., by 11.6% compared to the previous quarter. The third quarter itself recorded a decrease of 6.9% than its predecessor, and the fourth quarter of this year recorded a regression of 21.2% compared to its counterpart of 2005. The preliminary estimates indicate a dwindling in the GDP from \$4,442.7 million in 2005 to \$4,150.6 million in 2006, i.e., by an approximate rate of 6.6%.

This shrink was all around and in most of the economic activities, e.g., mining, manufacturing, electricity and water supply activity, construction, wholesale and retail trade, transport, storage, communications, real estate and rental activities, community, social and personal services, restaurants and hotels, education, health and social work, as well as in the sectors of public administration and defense.

Second: Economic Sectors

The available estimates of the performance of the economic sectors that constitute the GDP indicate a considerable fluctuation in the gross value added of all economic sectors in the fourth quarter of 2006, compared with both its predecessor and its counterpart of 2005, i.e., it increased and decreased by different rates.

1. Agriculture and Fishing

The available preliminary estimates indicate an increase of 14.8% in the gross value added to the agricultural and fishing sectors during the fourth quarter of 2006 compared with the previous quarter of the same year, i.e., from \$80.9 million to \$92.9 million. This was presumably due to the strike of the civil servants in the public sector which impelled some of them to temporarily engage themselves in agriculture, hence was the noticeable increase in agricultural products, particularly olives. The gross value added for this sector registered an increase of 20.6% in the fourth quarter of 2006 compared to its counterpart in 2005, i.e., from \$77 million to \$92.9 million. The preliminary estimates indicate an annual increase in the gross value added for the agricultural and fishing sector in the year 2006 compared to its counterpart of 2005. It increased from \$312.6 million in 2005 to \$334 million in 2006, i.e., an increase of 6.8%. This sector contribution to the GDP was 8%.

2. Mining, Manufacturing, Electricity and Water

The gross value added to mining, manufacturing, electricity and water supply activity, in the WB and GS during the fourth quarter of 2006 had shrunk by 7.8% than it was in the previous quarter of the same year, from \$144 million to \$133 million; while it had also slightly dwindled in the fourth quarter of 2006 compared to its counterpart of 2005, i.e., by less than 1%, from \$134 million to \$133 million. According to preliminary estimates, the annual gross value added for this sector shrank from \$564.8 million in 2005 to \$531.1 million in 2006, i.e., a decrease of about 6%. The sector contribution to the GDP was 12.8%. Out of the components of this sector, manufacturing was the largest, and its contribution to the GDP constituted 83.6%, that is \$444 million of the gross value added for this sector, while that of the water and electricity supplies was 13%, about \$69 million, followed by mining whose contribution was 3.4% i.e., a total of \$18 million.

3. Construction

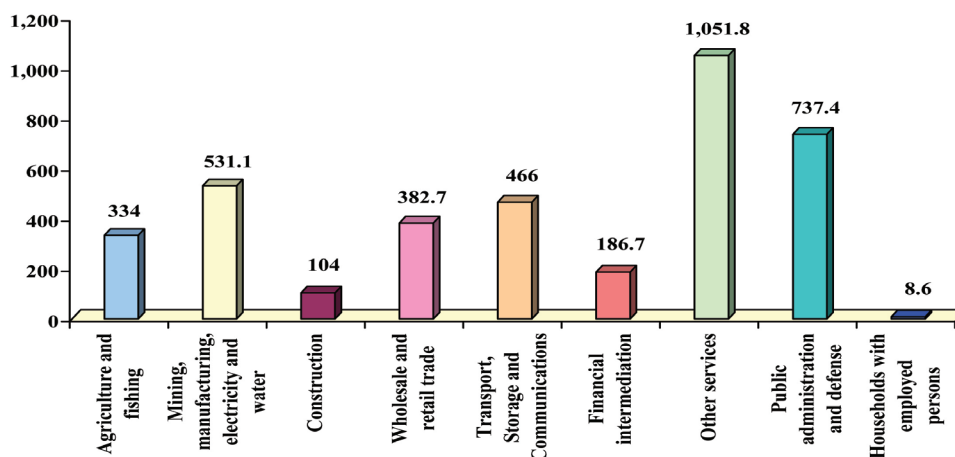
The gross value added to the construction sector had slightly decreased in the fourth quarter of the year 2006, compared to that of the previous quarter of the year, i.e., by 0.4%, from \$24.7 million to \$24.6 million. But this sector shrank by 14.3% compared to its counterpart quarter of the year 2005, i.e., from \$28.7 million to \$24.6 million. The annual value had also decreased from \$119.4 million in 2005 to \$104 million in 2006, a decrease of 12.9% approximately. This sector contribution to the GDP was 2.5%.

Table 1/9: GDP in the WB and GS by Economic Activity for the Quarters of Year 2006 at Constant Prices: 1997 is the base year (\$ million)

Economic activity	Annual data	Q I	Q II	Q III	Q IV
Agriculture and fishing	334	71.1	89.1	80.9	92.9
Mining, manufacturing, electricity and water	531.1	119.3	134.6	144.2	133
- Mining and quarrying	18	4	4.6	4.9	4.5
- Manufacturing	444	99.8	112.5	120.5	111.2
- Electricity and water supply	69.1	15.5	17.5	18.8	17.3
Construction	104	27.5	27.2	24.7	24.6
Wholesale and retail trade	382.7	92.3	93.9	102.8	93.7
Transport, storage and communications	466	121.7	114.5	115.8	114
Financial intermediation	186.7	46.9	46.2	46.8	46.8
Other services	1,051.8	291.5	296.4	254.2	209.7
- Real estate, renting and business services	447.8	107.4	107.8	120.3	112.3
- Community, social and personal services	43.3	11.1	11	10.8	10.4
- Hotels and restaurants	67	17.2	23.5	14.6	11.7
- Education	311.2	98.2	96.7	69.4	46.9
- Health and social work	182.5	57.6	57.4	39.1	28.4
Public administration and defense	737.4	220.9	202.4	184.1	130
Households with employed persons	8.6	2.2	2.2	2.1	2.1
Less: Financial Intermediation Services Indirectly Measured (FISIM)	-138.4	-34.4	-34	-34.7	-35.3
Plus: Customs duties	183.6	59.2	44.8	39.8	39.8
Plus: VAT on imports, net	303.1	93.4	85.9	66.8	57
GDP	4,150.6	1,111.6	1,103.2	1,027.5	908.3

Source: PCBS.

GDP in the WB and GS by Economic Activity 2006 (\$ million)



4. Wholesale and Retail Trade

The gross value added for the wholesale and retail trade registered a decrease of 8.9% in the fourth quarter of 2006, compared to the third quarter of the same year, i.e., from \$102.8 million to \$93.7 million. The sector had also experienced a slight decrease of 0.4% in the fourth quarter of 2006, compared to its counterpart of the previous year, 2005, that is from \$94.1 million to \$93.7 million. However, the annual value of this sector increased by 2.4%, from \$373.9 million in 2005 to \$382.7 million in 2006, and with a contribution of 9.2% to the GDP.

5. Transport, Storage and Communication

The gross value added for transport, storage and communication sector experienced a decrease of 1.6% during the fourth quarter of 2006, compared to the third quarter of the same year, i.e., from \$116 million to \$114 million. But the annual value of this sector had slightly increased by 1%, from \$461 million in 2005 to \$466 million in 2006. The percentage contribution for this sector to the GDP reached 11.2%.

6. Financial Intermediation

The gross value added for the various activities of financial intermediation was stable during the fourth quarter of 2006, compared to the third quarter of the same year, as the figure reached to \$46.8 million; but it shrank by 8.4%, compared to the counterpart quarter of 2005. As for the annual value of this sector, it registered a slight decrease of about 0.4% in 2006 compared to 2005, i.e., from \$187.4 million to \$186.7 million, and its contribution to the GDP was 4.5%.

7. Services

The gross value added for the various service activities recorded a decrease of 18% percent during the fourth quarter of 2006, compared to the third quarter of the same year, i.e., from \$254 million to \$210 million. The value of this sector had also decreased by 27% during the fourth quarter of 2006, compared to its counterpart of the previous year, 2005, i.e., from \$287 million to \$210 million. As for the annual value of the sector, it shrank from \$1,100 million by the end of 2005 to \$1,052 million in 2006, i.e., a decrease of 4.5%. The service sector contribution to the GDP of the year 2006 was 25.3%.

Real estate, renting and commercial services had the lion's share of its contribution in the year 2006, that is by a percentage of 42.6%, and with a total value of \$448 million that represented 10.8% of the GDP of the same year. However, the value of the sector decreased by 6.7% during the fourth quarter of 2006, compared to the third quarter of the same year, that is from \$120 million to \$112 million. As for the annual value of this sector, it slightly increased by 0.2%, from \$446.8 million in 2005 to \$447.8 million in 2006.

Education occupied the second position of all the activities of the service sector, as it contributed by 29.6% of the total contribution of this sector in 2006, i.e., \$311 million that represented 7.5% of the GDP of the same year. But the value of this sector had substantially decreased during the fourth quarter of the year 2006, compared to the third quarter of the same year, i.e., by 32%, an amount of \$22.5 million. A comparison of the value of this activity during the fourth quarter of 2006 with its counterpart of the year 2005 reveals a huge regression of 48.6%, that is from \$91 million to \$47 million. The annual value of this sector had also shrunk from \$342 million in 2005 to \$311 million in 2006, i.e., by 9%.

Health and social work occupied the third position of the service sector, as their annual value totaled \$182 million in 2006, which represented 17% of the annual value of the service sector, and 4.4% of the GDP of the year 2006. The value of this sector had decreased by 27.4% during the fourth quarter of 2006, compared to the third quarter of the same year, i.e., from \$39.1 million to \$28.4 million. But the value of this activity dwindled by 51.9% during the fourth quarter of 2006, compared to its counterpart of the year 2005, that is from \$59.1 million to \$28.4 million. A comparison of the annual value of this activity by the end of 2006 with that of the end of 2005 shows a regression of 8.6%, that is from \$199.6 million to \$182.5 million.

The activity related to restaurants and hotels occupied the fourth position of the service sector. Its annual value in the year 2006 was about \$67 million, which represented 6.4% of the annual value of the sector, and 1.6% of the GDP of the year 2006. The value of this sector had decreased by 20% during the fourth quarter of 2006, compared to the third quarter of the same year, i.e., from \$14.6 million to \$11.7 million. The value of this activity dwindled by 34.6% during the fourth quarter of 2006, compared to its counterpart of 2005, i.e., from \$17.9 million to \$11.7 million. The annual value of this activity had also shrunk by 1.5%, that is from \$68 million in 2005 to \$67 million in 2006.

The last activity of this sector is the social, societal and personal services. Its annual value in the year 2006 reached about \$43 million, which represented about 4% of the annual value of this sector, and around 1% of the GDP of the same year. The value of this activity in the fourth quarter of 2006 was approximately equal to its value in the third quarter of the same year, as the figure reached about \$10 million. Moreover, the annual value of this sector in 2005 and 2006 was almost the same.

8. Public Administration and Defense

The gross value added for public administration and defense recorded a 29.4% decrease during the fourth quarter of 2006, compared to the third quarter of the same year, which is from \$184 million to \$130 million. The value of this activity dwindled by 43.8% during the fourth quarter of 2006, compared to its counterpart of 2005, that is from \$231.2 million to \$130 million. Its annual value reached in 2006 about \$737 million, which represented 17.8% of the GDP of the same year. However, the annual value of this activity experienced a regression of 7.5% in the year 2006, compared to that of the previous year, that is from \$796 million to \$737 million. This regression was accompanied by a relative stoppage of government activities, particularly in the WB.

Third: The GDP per Capita

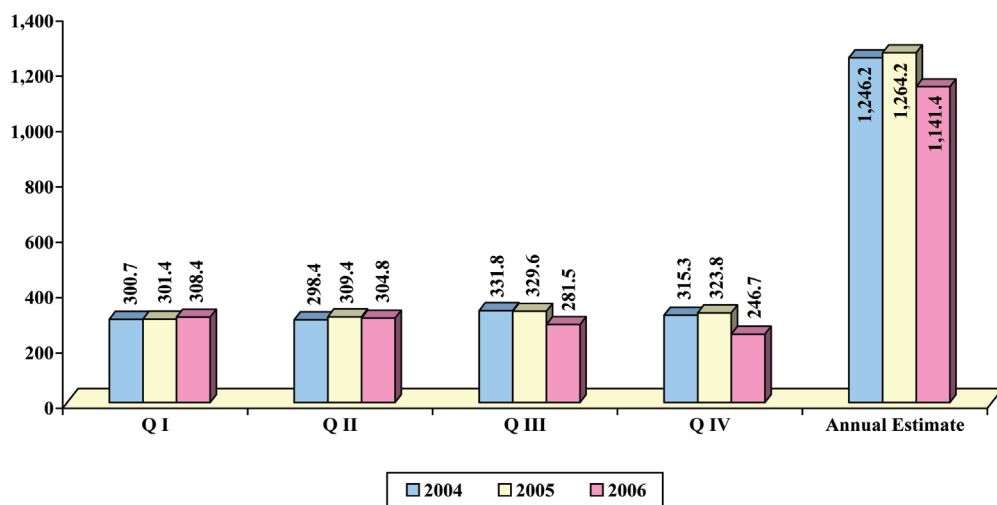
The following table 2/9, shows the changes in the GDP per capita in the WB and GS during the years 2004-2006, and at constant prices. According to preliminary estimates, it decreased in 2006 by 9.7%, compared to the previous year, 2005, that is from about \$1,264 to \$1,141.

**Table 2/9: GDP per Capita by the Quarters of Years 2004-2006
at Constant Prices: 1997 is the base year (\$)**

Quarter \ Year	2004	2005	2006
Q I	300.7	301.4	308.4
Q II	298.4	309.4	304.8
Q III	331.8	329.6	281.5
Q IV	315.3	323.8	246.7
Annual estimate	1,246.2	1,264.2	1,141.4

Source: PCBS.

GDP per Capita by the Quarters of Years 2004-2006 (\$)



Fourth: Public Finance

The successive political developments in the Palestinian territories during the year 2006 led to radical changes in all items of the budget. This was particularly so because of the unprecedented economic and financial siege that was imposed on the PA during the year 2006. It caused a serious financial crisis that had been reflected on the lives and performance of individuals and institutions, and had its repercussions on the public finance. This may be noted from an analysis of the components of the budget: revenues, expenses and internal and external funding.

Table 3/9: The Financial Status of the PA 2005-2006 (\$ million)

	2005		2006 (Actual)	
	Budget	Actual	Q I	Q II
Gross revenues	1,026.1	1,290.65	167.43	63.85
Domestic revenues	384.06	476.36	98.75	63.85
- Tax revenues	202.7	230.55	73.59	41.66
- Non-Tax revenues	181.36	245.81	25.16	22.19
Clearance	642.04	814.29	68.68	0
Vat refunds (-)	0	-82.07	0	-5.39
Net revenues	1,026.1	1,208.58	167.43	58.46
Gross expenditures and net lending				
Gross expenditure	2,027	1,649.84	370.25	374
Wages and salaries	907.79	1,000.96	277.1	288.77
- Civilian	547.97	626.05	163.41	168.25
- Security	359.82	374.91	113.69	120.52
Non-wage expenditure	859.29	614.2	92.38	83.76
PA financed capital spending	259.92	34.68	0.77	1.47
Net lending	126.08	274.86	60.8	30.04
Balance				
Balance	-1,126.97	-716.12	-263.63	-345.59
External budget support	1,162	348.53	157.76	102.27
Balance after external budget support	35.03	-367.59	-105.87	-243.32

Source: Palestinian National Authority/ Ministry of Finance.

Table 4/9: Preliminary Estimates of the Revenues and Expenditures 2006
(\$ million)

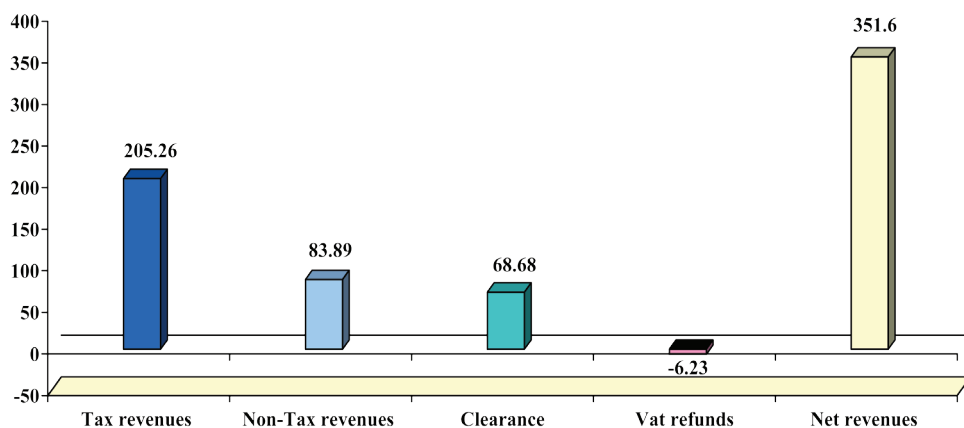
Gross revenues	357.83
Domestic revenues	289.15
- Tax revenues	205.26
- Non-Tax revenues	83.89
Clearance	68.68
Vat refunds (-)	-6.23
Net revenues	351.6
Gross expenditures and net lending	1,728.04
Gross expenditure	1,573.62
Wages and salaries	1,181
- Civilian	678.19
- Security	502.81
Non-wage expenditure	384.14
PA financed capital spending	8.48
Net lending	154.42
Balance	-1,376.44
External budget support	721.71
Total other financing	588.74
Net clearance revenue arrears accumulation	0
Net domestic bank financing	-100.3
Palestinian Investment Fund	184.24
Cash insurance/ Palestinian Investment Fund	11.05
Residual	493.75

Source: Palestinian National Authority/ Ministry of Finance.

1. Public Revenues

The released preliminary data on the financial performance in the year 2006 show a continuous shrink in the public revenues credited to the account of the Palestinian Ministry of Finance. This decrease started in the first quarter of 2006, but it became much more acute in the second quarter of the year. For the net revenues had decreased from \$167.4 million to \$58.5 million, respectively in the former and the latter quarters, that is by 65.1%. Compared to the second quarter of the year 2005, this dwindling reached to about 75%. This is also reflected in the figures of the net revenues, which decreased from \$1,208.6 million in 2005 to \$351.6 million in 2006, i.e., a decrease of 70.9%. An analysis of the main sources of the public revenues shows that the major reason for this dramatic shrink is the failure of the Israeli authorities to transfer the monthly clearance revenues to the Palestinian Ministry of Finance, which were sharply reduced from \$814.3 million in 2005 to \$68.7 million in 2006, that is a decrease of 91.6%. Tax revenues retracted from \$230.6 million in 2005 to \$205.3 million in 2006, i.e., an approximate decrease of 11%. Similarly, non-tax revenues recorded a decrease from \$245.8 million in 2005 to \$83.9 million in 2006, i.e., a decrease of 65.9%.

Preliminary Estimates of the Revenues 2006 (\$ million)



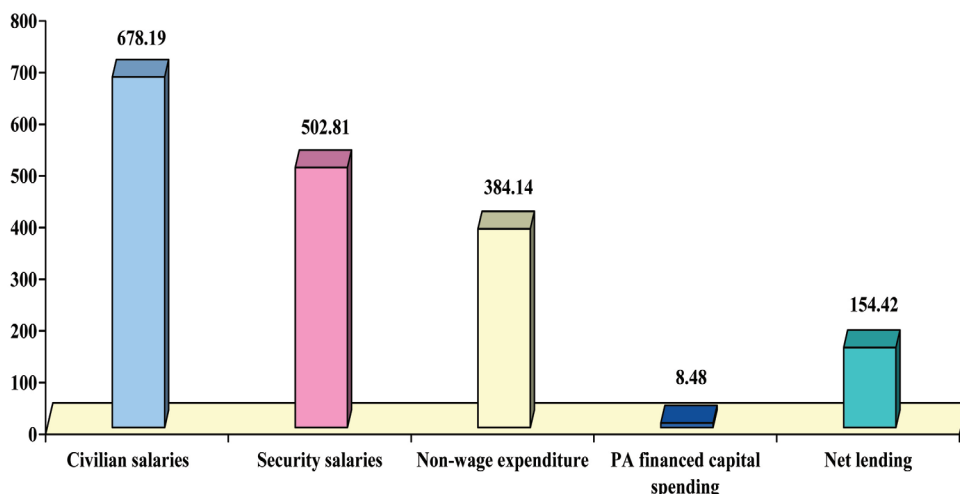
2. Public Expenditures

The decrease in revenues was bound to lead to a corresponding decrease in expenditures, which shrank from \$1,650 million in 2005 to \$1,574 million in 2006, i.e., a decrease of 4.6%. The item of the salaries alone represented 75% of the gross expenditure (\$1,181 million), which indicates that the PA has been the main

employer of the working forces, and that the item of the public expenditures of its budget is not flexible. The size of the non-wage expenditure had also decreased from \$614 million in 2005 to \$384 million in 2006, i.e., decrease of 37%. The PA financed capital spending was also reduced from about \$35 million in 2005 to approximately \$8.5 million in 2006, i.e., a decrease of about 76%. The huge decrease in the value of this item of the budget indicates apathy or insufficient funds allocated to projects and developmental plans. The net lending funds decreased from \$275 million in 2005 to \$154 million in 2006, that is a decrease of about 44%.

Thus, the budget of 2006 shows a deficit of \$1,376 million, compared to \$716 million in 2005. These figures show that the decrease in the 2006 revenues was much higher than the decrease in the expenditures in the same year.

Preliminary Estimates of the Expenditures and Net Lending 2006 (\$ million)



3. The Revenues of the Palestinian Authority

By 2006 the amount of taxes collected by Israel on behalf of the PA totaled about \$733 million, of which the Hebrew state handed to the PA before the formation of Hamas government \$68 million only. Meanwhile, the economic activities in the WB and GS declined, and consequently the gross revenues acquired by the PA were sharply reduced from \$1,290.7 million in 2005 to \$357.8 million in 2006, an overwhelming shrink of 72.3%.

Simultaneously with the stoppage of the flow of this fund, the donor states suspended their aid, which placed the Palestinian government into a desperate financial fiasco that compelled it to stop paying the salaries of the officials of the public sector, and to withheld essential services to the community.

The donors paid very little aid to the Palestinian government in the first half of 2006. However, by the second half of the year, the EU developed an alternative mechanism to extend aid to the Palestinian people directly and not via the channels of the Palestinian government. Through this so called the “Temporary International Mechanism (TIM),” that was implemented via HSBC Bank, the EU transferred \$140 million to finance the health services, and to pay part the cost of both the PA oil purchase from Israel and the salaries of the public sector’s officials.

Table 5/9: Donations of the Donor States 2005-2006

States	2005	2006
Total (\$)	1,189,151,934	718,767,116
Arab countries (%)	14	36
European Union (%)	46	33
North America (%)	20	12
Far East countries (%)	7	9
Other countries (%)	13	9

Source: These percentages were calculated using the figures of the Palestinian National Authority/ Ministry of Planning.

From the above table, it is clear that the donors’ aids had substantially decreased by 40% in 2006, compared to that of the previous year, 2005, that is from about \$1,189 million to \$718 million. The table also shows that the contribution of the Arab countries in the overall aid increased from 14% in 2005 to 36% in 2006, while that of the EU decreased from 46% in 2005 to 33% in 2006. Along the same pattern, the percentage of the American aid decreased from 20% in 2005 to 12% in 2006. Thus, there was a shifting in positions during the year 2006 in the sense that the Arab aid to the Palestinians became more important than its European counterpart. Besides, an important percentage of the aid was channeled through non-governmental channels.

However, statistics on foreign aid extended to the PA and the Palestinian people are rather conflicting, and should therefore be viewed cautiously. This is primarily due to the blockade that Israel, as well as the USA and its allies, imposed on the Palestinian people and the government of Hamas, which had, however, triggered the engineering of alternative mechanisms to extend the funding without passing through the Palestinian Ministry of Finance. Hence, most of the funds found their way to non-governmental institutions and agencies, which made it difficult to know their exact amounts, and opened the doors for financial corruption.

The above mentioned total foreign aid of \$1,189 million in 2005 included some \$350 million that the donors paid to support the PA's budget for the year, and the rest of the aid funded projects and the infrastructure. But the donors' aid for the year 2006, about \$718 million, was, in fact, directed to support the PA's budget, which explains the claim of the World Bank and the UN that the aid extended to the PA in the year 2006 had doubled, though the International Monetary Fund (IMF) estimates this aid by about \$747 million. According to the statistics of the IMF, the Palestinian government received \$234 million, of which \$181 million were from Arab countries, President 'Abbas' Office got \$291 million of which \$275 million were from Arab countries, \$172 million came from the TIM and \$49 million via the Interim Emergency Relief Contribution (IERC) of the European Commission (EC).

European sources, like the website of the British Foreign Office, helps us to understand the size of the aid extended to the Palestinian people without passing through the government or the presidency. These sources mention that the EU extended to the Palestinians in the year 2006 a sum of 680 million euros (about \$815 million). Other sizeable funds were received from Iran, the Arab and Muslim masses and from philanthropic organizations that had all contributed in supporting the struggle of the Palestinian people, and in funding different projects. Thus it is not surprising that Salam Fayyad, the finance minister of the government of national unity, estimated the foreign aid for the year 2006 as \$1,350 million. These funds had to some extent compensated the tax funds that were withheld by Israel, and minimized the catastrophic repercussions of the blockade. Hence most of this aid was spent on humanitarian aspects and not included in the PA budget or its projects. While 16% of the European aid was allocated for humanitarian purposes in the year 2005, the figure jumped to 56% in the year 2006. Similarly, government expenditure on projects was reduced from \$330 million in 2005 to only \$180 million in 2006.

4. The Palestinian Authority Debt

Up to the end of 2006, the PA debt totaled \$1,772 million of which \$1,061 million were foreign debts, \$66 million were banks' installments and interests, \$550 million were overdrafts to banks and \$95 million were other expenditure. All that was paid of this debt was about \$150 million.

It is known that bank loans are subject to compound interest, thus the service of these loans constituted another burden on the budget. Some banks tended to confiscate part of the funds credited to the account of the PA in order to reduce this debt, which aggravated the crisis of liquidity.

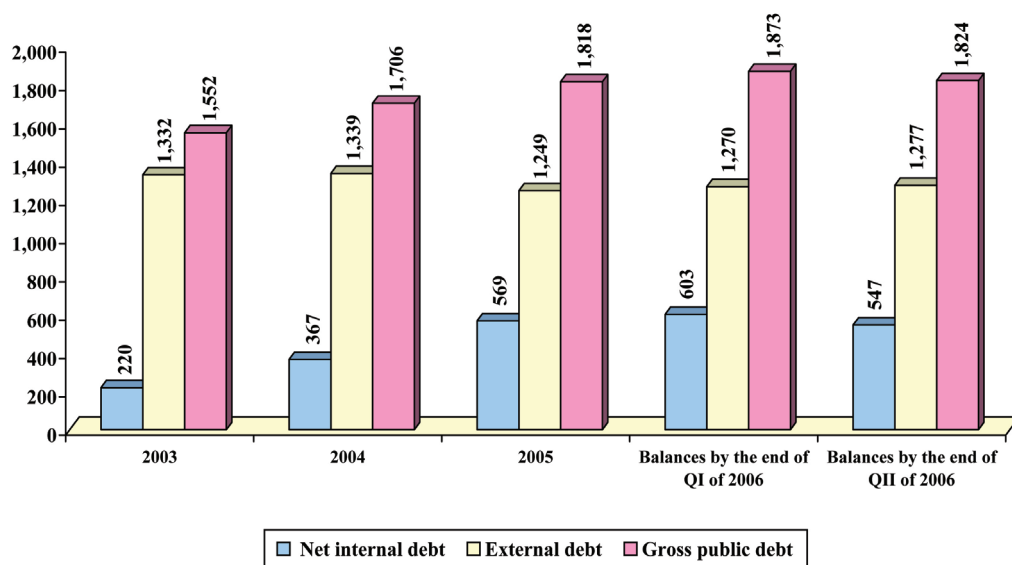
The arrears of the salaries totaled by the end of 2006 about \$550 million, while those of the Insurances and Pensions General Corporation were about \$311 million, most of which belonged to earlier periods as they were not regularly paid.

Table 6/9: The Status of the Public Debt 2003-2006 (\$ million)

	2003	2004	2005	Balances by the end of QI of 2006	Balances by the end of QII of 2006
1. Net internal debt	220	367	569	603	547
2. Foreign debt	1,332	1,339	1,249	1,270	1,277
3. Gross public debt (1+2)	1,552	1,706	1,818	1,873	1,824

Source: Palestinian National Authority/ Ministry of Finance.

The Status of the Public Debt 2003-2006 (\$ million)



Fifth: The Palestinian Banking Sector

Notwithstanding the tremendous financial constraints and the imposed blockade on the Palestinian territories in the WB and GS, the Palestinian banking sector was on the whole functioning and stable. The bank reserves were maintained, they totaled about \$5,570 million by the end of September 2006. In the circumstances, this was a positive indicator.

The deposits in the banks totaled \$4,560 million, of which \$394 million were inter-banks deposits, while the bank facilities reached about \$1,890 million. The number of the functioning banks in the Palestinian territories in the year 2006 remained as it was in 2005, that is 21 banks with 146 branches.

Table 7/9: Development of the Functioning Banks and their Branches in Palestine 2004-2006

Year	No. of the functioning banks	No. of branches
2004	22	135
2005	21	141
2006	21	146

Source: Palestinian Monetary Authority (PMA), data not published.

The Palestinian Monetary Authority (PMA) was established in 1995 to supervise all the banks in the Palestinian territories, and to administer the monetary policy of the PA. However, the latter function was suspended because of the lack of a Palestinian currency and the circulation of three different currencies, the dollar, the Jordanian dinar and the Israeli shekel. Hence the function of the PMA was confined to the supervision of banks, as it was unable to take any measures on the monetary policy. However, the PMA tried its utmost best to consolidate the security and strength of the banking sector. It took the necessary measures to ensure its efficiency and effectiveness according to international standards.

The Palestinian banks had experienced during the year 2006 a serious financial and security crisis because of the blockade, and the continuous threat of American and international sanctions on all banks that deal directly or indirectly with the Palestinian government, which compelled them to stop dealing with the Palestinian government, and to refrain from accepting any outside funds transferred to its account.

**Table 8/9: Banks Deposits and Facilities in the Palestinian Territories
2001-2006 (\$ million)**

Year	2001	2002	2003	2004	2005	2006
Deposits	3,398	3,430	3,624	3,957	4,331	4,166
Facilities	1,220	950	1,065	1,420	1,712	1,890

Source: Palestinian Monetary Authority (PMA).

The above table 8/9, shows the status of the deposits and facilities in the Palestinian banking sector during the period 2001-2006. Despite the blockade and the tremendous financial constraints in the Palestinian territories, the table indicates that the bank deposits increased from \$3,398 million in 2001 to \$4,166 million in 2006, i.e., an increase of 22.6%. As for the bank facilities, they totaled \$1,890 million in mid 2006. Their size increased by 10% and 55% compared to the years 2005 and 2001 respectively. 27% of the total of these facilities were allocated to the public sector, and 72% to the private sector. The loans constituted the major part of these facilities, about 63%, followed by facilities for current debts, which constituted 36%. The facilities offered in US dollar had the lion's share of these facilities (70%), followed by the Israeli shekel (17%) and the Jordanian dinar (12%).

Sixth: Consumer Price Index

According to the statistics of the PCBS, the consumer price index in the Palestinian territories increased by 3.76% during the year 2006, compared to 2005, as the consumer price index (base year 1996=100) increased to 152.31 in 2006, compared to 146.79 in the previous year. This increase was more than that of 2005, which witnessed an increase of 3.47% compared to the year 2004.

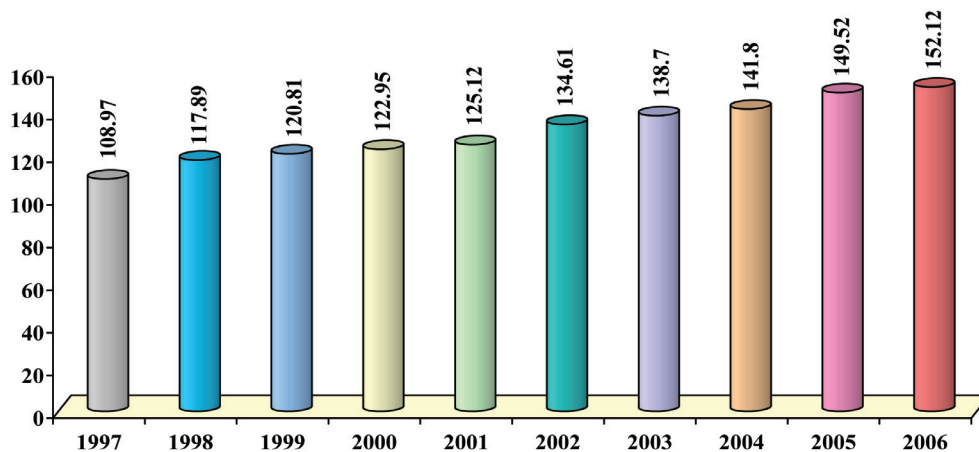
The PCBS alluded this increase to an all around increase in the prices: miscellaneous goods and services by 5.6%, transport and communications by 5.57%, food by 4.86%, beverages and tobacco by 3.29%, housing by 3.27%, Education by 1.55%, medical care by 1.51%, and furniture, household goods and services by 1.4%. Form these figures, it is clear that the increase in the prices of food, and transport and communications as well as miscellaneous goods and services was the direct reason for this increase in the cost of living.

**Table 9/9: The General Trend of the Consumer Price Index
for the Month of October 1997-2006**

Year	Consumer Price Index
1997	108.97
1998	117.89
1999	120.81
2000	122.95
2001	125.12
2002	134.61
2003	138.7
2004	141.8
2005	149.52
2006	152.12

Source: PCBS.

The General Trend of the Consumer Price Index for the Month of October 1997-2006



Seventh: The Standards of Living

Preliminary statistics indicate a profound deterioration in the living and economic conditions during the year 2006. The Palestinians suffered from an unprecedented Israeli siege that was caused by their detention of the PA's dues, closure of the passages and obstruction of trade from and to the Palestinian territories. Additionally, was the external blockade represented primarily by the prohibition of the transfer of funds to the Palestinians of the interior, be it charities, aids or loans. The USA and the European powers compelled all the banks and financial institutions in the Palestinian territories to stop transferring funds to the Palestinian territories, otherwise American and European central and commercial banks as well as other world banks will stop dealing with them. Besides, countries that were willing to extend financial aid to the Palestinian people were unable to do so because of the intense American pressure and threats. Hence the government failed to pay the salaries of the Palestinian workers, the Palestinian capital fled the land and factories as well as commercial and industrial institutions were closed down. These adverse developments curtailed foreign investment in the territories, increased poverty and unemployment and reduced the standard of living of the interior Palestinians throughout the year 2006. Statistics indicate that the percentage of the Palestinian families living below the poverty line increased

from 50% in March 2006 to 68% in November of the same year. The economic and living conditions in GS were worse than those in the WB. In GS 79% of the inhabitants lived below the poverty line, where 51% of them lived in extreme poverty. Conversely, in the WB 61% were under poverty line where 28% of them experienced extreme poverty.

Eighth: The Salaries' Crisis

Due to the financial and economic blockade imposed on the Palestinian territories throughout the year 2006, the government failed to pay the salaries of the employees of the public sector. The monthly salaries and similar payments totaled \$120 million, of which the salaries alone were \$100 million. In 2006, the salaries constituted 75% of the gross expenditure, compared to 60% in 2005. For the salaries in 2006 totaled \$1,181 million, compared to \$1,000 million in 2005. This increase in the salaries and wages was due to the increase of the employees from 140,500 officials by the end of June 2005 to over 160,000 officials by the end of June 2006, that is an increase of about 14%, who were employed by the predecessor of Hamas government. However, the Palestinian government paid the salaries in installments until November 2006. The government concluded an agreement with the Government Employees Union by which it undertook to pay the salary arrears, about \$500 million, in four installments and on the availability of funds.

About half of the Palestinian families (51.6%) maintained that they had been directly or indirectly affected by this salary crisis (26.6% were affected directly and 25% indirectly). The percentage of the families affected by this salary crisis in GS (72.7%) was more than that in the WB (40.6%). These results are coherent with the degree of dependence on public posts in both regions.

Table 10/9: The Numbers of the Employees of the PA for Different Periods 2005-2006

	Civilian	Military personnel	Military personnel under experiment	Total excluding military personnel under experiment	Total including military personnel under experiment
January 2005	75,766	57,067	5,469	132,833	138,302
June 2005	78,744	57,067	4,676	135,811	140,487
December 2005	79,705	57,067	13,966	136,772	150,738
January 2006	79,722	57,067	20,839	136,789	157,628
February 2006	80,786	57,067	20,584	137,853	158,437
March 2006	81,043	57,067	20,793	138,110	158,903
April 2006	81,007	57,611	20,712	138,618	159,330
May 2006	81,079	58,388	19,816	139,467	159,283

Source: Palestinian National Authority/ Ministry of Finance.

Ninth: The Labor Market

The statistics of the PCBS indicate that the percentage of participants in labor force has increased by 1% during the period between the second and third quarters of 2006, that is from 40.9% to 41.3%. Moreover, the participation rate of women in the workforce increased from 13.7% in the second quarter of 2006 to 13.9% in the third quarter, i.e., an increase of 1.5% (equivalent to three thousand women).

In line with the broad definition of unemployment, the statistics indicate an increase in the numbers of the unemployed (whether they are seeking or not seeking for jobs), i.e., from 28.6% in the second quarter to 30.3% in the third quarter of the year 2006. The statistics also show an increase in the percentage of unemployment in both the WB and GS. It rose in the WB from 18% in the second quarter of 2006 to 19.1% in the third quarter of the same year, while in GS it rose during the same quarters from 34% to 36.3%. The highest percentage of unemployment was among the youngsters. The highest rate was amongst the age group 20-24, it reached 38.7% (32.3% in the WB and 53.7% in GS), followed by the age group 15-19 which reached 32.6% (28% in the WB and 49.2% in GS), and lastly the age group 25-29 which reached 25.9% (20.5% in the WB and 37.1% in GS).

The statistics show an increase in the number of employed persons between the second and third quarters of 2006, as it increased by two thousand workers to be 664 thousand workers in the third quarter. The numbers of the employed persons in the WB increased by eight thousand workers, while it decreased in GS by six thousand workers, to be 497 thousand workers in the WB and 167 thousand in GS. Moreover, the number of employed women in the Palestinian territories decreased from 116 thousand to 110 thousand. The statistics of the PCBS show that 22.6% of the overall employees are employed by the public sector (15.4% in the WB and 44% in GS).

Statistics also show that the average value of the nominal daily net wage of the employees in the WB, increased slightly from \$17 in the second quarter of 2006 to \$17.5 in the third quarter of the same year, while it decreased in GS during the same period, from \$15.6 to \$15.4.

Tenth: Palestine Securities Exchange

The political developments in the Palestinian territories had negative impact on the performance of the Palestine Securities Exchange (PSE) during the year 2006. *Al-Quds* Index, which opened at 1,128 points on 2/1/2006, started on a dramatic downward trend. By 24/1/2006, the last trading session before the legislative elections, the Index had declined to the 1,073 points.

This severe drop impelled the Capital Market Authority (CMA) and the PSE to take a number of measures, of which the most important was to reduce the amount of intraday stock price fluctuation from 5% to 3%, starting from the trading session on 21/3/2006. But this percentage was reversed to what it previously was since 14/8/2006 because *al-Quds* Index showed relative stability.

With preliminary election results on 26/1/2006, indicating Hamas victory, the first trading session held after the elections witnessed a 51 point decline on *al-Quds* Index. In the days that followed, the Index continued to post maximum allowed daily losses each trading session. Throughout the year, the political developments had become the primary factor that governed *al-Quds* Index, which did not reflect the actual performance of the market's companies of which the majority continued to achieve profits, though at a lower rate than those of the corresponding periods of 2005.

Correspondingly, with the political developments, the Palestinian bourse experienced some important developments in 2006 that had historical impacts on the movement of *al-Quds* Index, which all in all had been pushed downwards. The Index had acceleratingly declined to reach 495 points on 16 July, four days after the Israeli war on Lebanon. However, after the stoppage of the war and the appearance of signs of calm in the Palestinian arena, the Index rose to over 600 points. The overall loss of *al-Quds* Index during the year 2006 was 523 points, i.e., a decline of 46% compared to a rise of 306% in the year 2005.

The average daily trade volume declined by 39% to reach 0.92 million shares daily in 2006, compared to 1.5 million shares daily in 2005. The average daily trade value also decreased by 48% to reach \$4.41 million daily in 2006, compared to \$8.5 million daily in the year 2005.

All in all the total annual trade volume was reduced from 370 million shares in 2005 to 223 million shares in 2006, and the total annual trade value also shrunk to about a one billion dollars in 2006, compared to \$2 billion in 2005.

With regard to the sectors, the service sector had the lion's share, about \$455 million, which constituted 43% of the PSE's total trading value. The investment sector came in the second position, as it reached \$417 million, that is 39% of the PSE's total trading value. The banking sector had the third position with a fund of \$121 million, which constituted 11% of the PSE's total trading value. The share of the manufacturing and insurance sectors was \$55 million for the former, i.e., 5% of the PSE's total trading value, and \$20 million for the latter, that is 2% of the PSE's total trading value.

Eleventh: The Foreign Trade

With its exports and imports components, foreign trade is tremendously important for the Palestinian economy. It directly affects all economic sectors, the balance of payments and the prices. It also serves to avail the needs of the local market, such as ready-made commodities and raw materials, and to sell Palestinian products in external markets.

Since the Israeli occupation of the Palestinian territories, the foreign trade was associated with the developments in Israeli politics, economy and security. Due to the oppressive Israeli practices, the Palestinian economy was annexed to the Israeli

economy, and the Palestinian market became an open consumer market for Israeli products. These Israeli measures affected the nature and the size of trade between the Palestinian territories and the outside countries.

The balance of trade suffers from this inferior status of the Palestinian foreign trade, particularly the inability of the Palestinian exports to cover the cost of the imports. In fact, they provide less than 20% of the cost of the imports. The share of the trade with Israel was 80% of the total PA foreign trade. This reflects the overwhelming control of the Israeli economy over its Palestinian counterpart. About 92% of the total Palestinian exports go to the Israeli market, mainly to provide raw materials for the Israeli industries, and over three quarters of the total Palestinian imports come from the Israeli market, which constitutes 10% of the total Israeli exports to the outside world.

The imposed comprehensive Israeli siege on the Palestinian territories during the year 2006 had a tremendous impact on the Palestinian foreign and transit trade. All economic sectors were adversely affected by this blockade, particularly the agricultural and industrial sectors.

The following table, issued by the PCBS, gives preliminary statistics of the size of the Palestinian foreign trade with world countries for the year 2005.

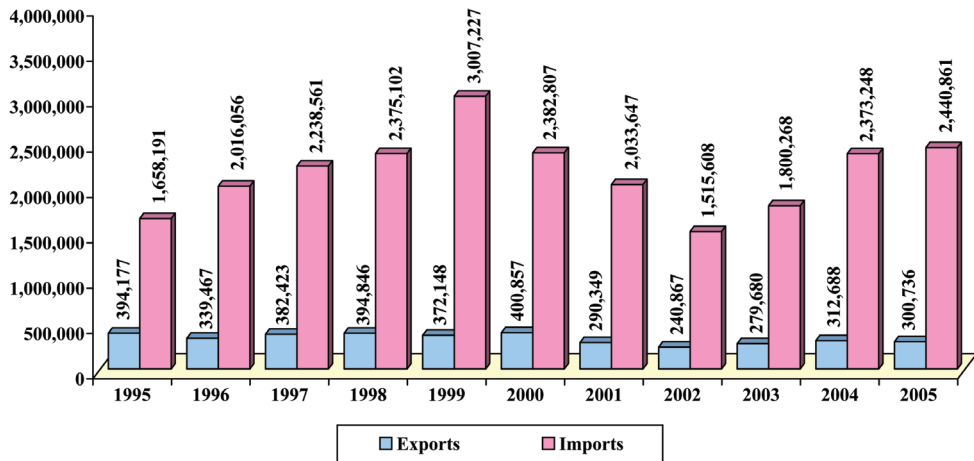
Table 11/9: Total Value of Exports, Imports, Net Balance and Transaction Trade for the WB* and GS according to the PCBS 1995-2005 (\$ thousand)

Year	Total value of exports	Total value of imports	Net balance trade	Transaction trade
1995	394,177	1,658,191	-1,264,014	2,052,368
1996	339,467	2,016,056	-1,676,589	2,355,523
1997	382,423	2,238,561	-1,856,138	2,620,984
1998	394,846	2,375,102	-1,980,256	2,769,948
1999	372,148	3,007,227	-2,635,079	3,379,375
2000	400,857	2,382,807	-1,981,950	2,783,664
2001	290,349	2,033,647	-1,743,298	2,323,996
2002	240,867	1,515,608	-1,274,741	1,756,475
2003	279,680	1,800,268	-1,520,588	2,079,948
2004	312,688	2,373,248	-2,060,560	2,685,936
2005	300,736	2,440,861	-2,140,125	2,741,597

* Excluding East Jerusalem that was annexed to Israel.

Preliminary Data/ PCBS.

Total Value of Exports and Imports for the WB and GS according to the PCBS 1995-2005 (\$ thousand)



The PCBS seems to have employed a different method in counting the exports and imports for the year 2006, which could not be compared with those of the previous years because of the differences in the scales and the methods of estimates. Hence, the initial figures given by the PCBS are almost similar to those of the International Monetary Fund (IMF), but largely different from the figures given by Palestinian sources in previous years. However, admittedly the Palestinian statistics bodies face formidable difficulties from two directions, namely their operation under Israeli occupation, and the inability of the PA to fully control the flow of commodities through the frontiers and the passages. In any case, the preliminary figures of the PCBS in 2006 are \$581 million for the exports and \$3,631 million for the imports, while those given by the IMF are correspondingly \$534 million and \$3,479 million. Since the IMF followed the same method of the previous years, we provide below for the sake of comparison a table for the years 1999-2006.

Table 12/9: Total Value of Exports and Imports for the WB* and GS according to the IMF 1999-2006 (\$ million)

Year	1999	2000	2001	2002	2003	2004	2005	2006
Exports	892	867	560	465	465	535	588	534
Imports	3,805	3,404	2,704	2,536	2,844	3,279	3,597	3,479

* Excluding East Jerusalem that was annexed to Israel.

Total Value of Exports and Imports for the WB and GS according to the IMF 1999-2006 (\$ million)



Twelfth: The Economic Development Potentials of the Palestinian Territories

Most of the experts in the Palestinian economy are of the opinion that there can be no real and sustainable economic development in the Palestinian territories under the Israeli occupation. Nonetheless, active effort should continue to find economic, political and other strategies to resist the occupation, and to stick to the homeland.

We may plausibly argue that the existence of effective developmental plans should in essence improve the standard of living of the Palestinian people through investment projects that increase production and provide job opportunities, which, in turn, will strengthen the resistance to the occupation. Experience had demonstrated that development largely depends on the existence of a

sound economic vision and good governance. However, in the Palestinian case such a vision requires a proper and scientific understanding of the economic infrastructure, including elements of its weakness. It should also take on board the security and political realities in the Palestinian territories in the WB and GS, where the occupation has systematically been engaged in the destruction of the Palestinian economic potentialities through a prolonged blockade, and by the Wall that isolates the Palestinian regions from each other, which had all accelerated the rate of poverty and unemployment, and diminished the real income of the peoples.

After the conclusion of the Oslo Accords in 1993, and the subsequent formation of the PA, it was generally hoped that economical and developmental plans would be drawn to achieve sustainable development in the Palestinian territories. But nothing of this sort took place. On the contrary, the Palestinian developmental vision has since 1994 been blurred, confused and chaotic. It failed to achieve its basic objectives, be it domestic strength, the removal or minimizing of economic and social tension that has accumulated during the long years of occupation or to reduce the dominance of the Israeli economy over its Palestinian counterpart, and to increase the linkage of the latter with Arab economies.

A viable and sustainable Palestinian developmental vision should be based on the Palestinian excellent human resources, the high expertise of the Palestinian people, and the vitality and dynamism of the Palestinian society, particularly in the fields of development and community service. Besides, the experience and the capital of over five million Palestinians in the diaspora constitute an important asset for achieving economic progress in the Palestinian territories. If attracted, their huge capital and distinguished expertise will be most useful for all developmental projects.

The absence since 1967 of a national government in the WB and GS has been instrumental in the prominence of the private sector as an important vehicle for development in these territories. Despite the formidable predicaments that the Israeli occupation has placed in the path of this sector, it continued to invest in service, agricultural and manufacturing projects, which, in turn, have contributed in the development of the economy of the occupied Palestinian territories.

The Palestinian economy suffers from a number of weaknesses that should be taken in consideration in any developmental plan. Most importantly is the weakness of the governmental sector that lacks sufficient expertise and ability to extend

good, effective and reliable services. For the PA has not given due attention to the establishment of sound, modern and transparent institutions. Another major factor for the weakness of the Palestinian economy is the continuation of the occupation, which delayed, even after the establishment of the PA projects, including strategic projects such as airports, water and electricity projects, digging of wells and the construction of highways in the Palestinian territories. Additionally, are the blockade and the Israeli control of the passages that paralyzed the movement of peoples and goods, isolated the Palestinian economy from the world economy and delayed developmental plans. This led to basic defects in the structure of the Palestinian economy, notably its submission to the Israeli economy and the weakness of the infrastructure.

Amongst the factors for the weakness of the Palestinian economy is the poverty of the WB and GS, which lack natural water and mineral resources that are essential for the success of developmental plans.

A Palestinian developmental vision should be squarely based on the abundant and highly professional Palestinian human resources, and has to be part and parcel of the Arab economy, and to open up to the regional as well as the international markets.

Thirteenth: Termination of the Linkage of the Palestinian Economy to the Israeli Economy

The Israeli control over the Palestinian territories took several forms, of which some are similar to those in former colonies, while others have their own specific characteristics. As was the case in traditional colonialism, Israel had previously focused on the exploitation of Palestinian labor, and the imposition of trade partnership that made the Palestinian territories a natural market for Israeli products. The special features of the Israeli colonialism are, on the other hand, represented by the control of lands and sources of water through confiscation of lands, establishment of settlements and the imposition of restrictions on the usage of water by the Palestinian farmers and citizens.

This Israeli economic imperialism, which is based on the amalgamation and destruction of the economy of the Palestinian territories, aims at the termination of

the Palestinian reality on the ground. Such a drive requires a counter and capable economic strategy that would defend the Palestinian economy as well as the Palestinian existence and identity.

After the conclusion of Oslo Accords in 1993 and the Paris Protocol, the Palestinian economy in the WB and GS should have presumably moved towards disengagement from its Israeli counterpart. But in reality the Accords maintained Israeli control over 60% and 40% of the lands of the WB and GS respectively, as well as on most of the water sources, all the trade, internal and external, and the movement of peoples. Additionally, the Paris Protocol allowed Israel to continue its control over the Palestinian economic fundamentals, and to limit the rights of the PA to undertake economic development for the benefit of its Palestinian people.

What added insult to injury was the failure of the PA to make use of the limited opportunities, and its lack of a vision and a work plan to overcome the predicaments, and establish a relatively independent Palestinian economy. It neglected its duty to play a positive and independent role to support the process of development and reconstruction, and to pursue developmental policies that would consolidate self-capabilities, strengthen the social cohesion of the Palestinian society, and link the Palestinian economy with its Arab environment.

The disengagement of the Palestinian economy from its Israeli counterpart is admittedly difficult, but this does not negate the availability of viable opportunities to start achieving this goal gradually and systematically. The starting point may be to strengthen the Palestinians' self-capabilities, particularly in the economic field, develop the human resources in a way that achieves the developmental vision, initiate measures to remove the defects of the economic and social environment, and to promote knowledge and technology. The PA should also restructure its own institutions in a professional manner, encourage local and foreign investment, and to start amalgamating the Palestinian economy with the Arab economy and to make use of the available opportunities in the major markets. The PA has also to diligently and speedily work for the amendments of the articles in the Paris Protocol that restrict the movement of the Palestinian economy, in order to associate it with the Arab, regional and international economies.

Conclusion

The core of the current complicated problems of the Palestinian economy in the WB and GS is the repugnant Israeli occupation and its aggressive policies and measures, which, in effect, have turned the WB and GS into a big prison. Moreover, they enable the occupiers to easily abort any developmental plan or economic reforms, destroy projects and the infrastructure and to control land, sea and air exists.

During the year 2006, the occupation had done its utmost best to tighten the blockade on the Palestinian people to destroy their will, and to punish them for their democratic option. Hence, compared to the previous year, the GDP decreased by 6.6%, the collection of taxes and governmental dues dwindled by 72%, the employment and capital expenses retracted by 37.5%, the developmental expenses dwindled by 75.5%, and the government managed to pay only about half of the salaries of its employees.

Nonetheless, one may bet that the Palestinian economy will not ultimately develop as long as it is under hostile hegemony. But this does not provide an excuse for any laxity in fighting all forms of financial corruption that appeared during the last years or in making the utmost possible use of the outstanding human resources of the Palestinian people. In fact, this assessment should motivate the Palestinian to build a resistance economy that can operate as best as possible in the prevailing conditions of the occupation.

The Israeli battle to break the will of the Palestinian people will continue as long as the occupation is controlling the destiny of Palestine, and the occupiers will never shy from using all ways and means to do this, including the food weapon. Thus, the PA should make the utmost best of the available resources as well as the donations and the foreign funds in order to consolidate the steadfastness, break the blockade and end the occupation.

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