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**The Economic Challenge in the Palestinian Authority following  
COVID-19**

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**The Palestinian Authority's efficient and rapid response to the coronavirus outbreak underscored the Gordian knot tying it to Israel in matters of geography, economy, civilian affairs, security, and health. Israel's new government would do well to recognize this, and consider the PA's stable and effective performance as a critical component of Israeli national security. The ability of the PA to advance economic growth in the West Bank is a central component of this Israeli interest.**

With the emergence of the coronavirus in the West Bank in early March 2020, the Palestinian Authority responded quickly and worked to contain the outbreak, treat those infected, improve its health services, and prevent the possibility of economic collapse. From the outset, the policy was driven first and foremost by medical considerations, including a state of emergency declared on March 5. The PA's response proved effective, and this in turn boosted the support for it among the Palestinian public. The numbers of ill and deceased persons are significantly lower than the numbers in Israel, and demonstrate the success of the PA's policy. This is especially remarkable given the weakness of the Palestinian medical system, overcrowded neighborhoods and refugee camps, poor civilian infrastructure, and the extensive interaction with Israeli citizens among Palestinian laborers who work in Israel and return to the West Bank. The PA's accomplishments were also enabled by effective cooperation with Israel and the understanding that in the absence of a defined and circumscribed border between the West Bank and Israel, the fates of Israelis and Palestinians are tightly linked. At the outbreak of the pandemic, an Israeli-Palestinian team was created that included officials from both health ministries, and the Coordination of Government Activities in the Territories (COGAT) administration began working with international organizations to improve the Palestinian health system. Now that the danger from the virus appears to be receding, the PA faces another momentous challenge – salvaging its economy.

The Israeli security paradigm holds that improvements in the economic situation in the PA, together with the Palestinian economy's significant dependence on Israel, contribute to stability and calm. At the same time, restrictions enacted by Israel to prevent undesired behavior, such as the recent implementation of the 2019 law on withholding funds

(“salaries”) paid to terrorists, undermine the PA’s economic stability and its ability to govern. During the coronavirus-induced financial crisis, the security situation in the Palestinian territories becomes even more precarious. The contrarian position of Palestinian Prime Minister Mohamed Shtayyeh does not help matters and fuels the contention. In response the implementation of the law, he initiated a process of economic severance: an attempt to redirect trade with Israel to other partners in order to reduce and even eliminate all economic relations. Already in the early stages this move exacted a high cost of the PA and led to salary cuts in the public sector.

In 2018 the PA's annual budget was NIS 17 billion: 60 percent (approximately NIS 10 million per year) comes from tax clearance payments collected and transferred by Israel, as formulated in the Paris Protocol; Israel is the destination for some 80 percent of manufacturing exports from the West Bank (worth approximately NIS 3 billion per year); it is likewise the source of employment for some 150,000 Palestinians who worked in Israel and the settlements prior to the pandemic, of whom only one-third have returned to work. The PA also relies on aid from donor countries (approximately NIS 2.5 billion in 2018), but this was slashed over the past two years due to moves by the Trump administration to cut aid to the Palestinians and legislation to prevent funding for terrorism. UNRWA's budget was also severely affected by American defunding, thus further reducing the assistance provided by the organization to the Palestinian public.

It is too early to assess the extent of the damage from the pandemic on the PA's economy, but forecasts are not encouraging. While the IMF's current global growth forecast for 2020 is -3 percent, the forecast by the *Economist's* research unit for the West Bank and Gaza is -8.5 percent. Shtayyeh announced that the PA's budget deficit, currently \$1.4 billion, is expected to reach \$3.1 billion by the end of the year – assuming that foreign aid payments will not be affected by the global crisis. The Palestine Monetary Authority and Palestinian banks have come to the assistance of the PA, but their influence is limited given the constraints of the Paris Protocols on the Palestinian financial system. Thus it cannot perform actions such as printing money, changing interest rates, or reducing exchange rates, and it lacks access to international capital that could finance its deficit. Palestinian banks are also under pressure not to transfer salaries to incarcerated terrorists or released prisoners, so as not to be exposed to lawsuits from terror victims.

This means that without major support from donor countries or from Israel, the PA will not be able to launch public projects that can jumpstart its economy. This situation will influence its ability to pay salaries to the public sector, which includes public health workers and security personnel – two critical components for Israel's security – and threatens the future of its very existence.

Against this background and in light of the pandemic, US Ambassador to Israel David Friedman announced on Twitter that the US administration would immediately transfer \$5 million to Palestinian hospitals and households for lifesaving aid. This comes after a cessation of more than \$200 million in aid payments since August 2018. Israel also realized the dire need caused by the pandemic and came to the assistance of the PA: On March 22, NIS 120 million – a surplus in tax revenues from recent years that were subject to long negotiations – were released to the PA; on April 12, a “loan” of NIS 500 million (which most likely will not be paid back) was approved to help the PA contend with the crisis; on May 10, then-Finance Minister Moshe Kahlon approved an advance of NIS 800 million of tax revenue payments, in four monthly installments. On the other hand, on April 26 the District Court in Jerusalem issued a temporary confiscation order on some NIS 450 million in response to claims filed by terror victims. In view of the scale of the need and the potential harm, intensified by fewer employment opportunities in Israel, these contributions by Israel and the US are far from sufficient to halt the economic collapse of the PA, especially since it is still unknown when and how the pandemic will end.

### **Implications for Israel**

While the Israeli government tries to pressure the PA to stop funding prisoners and cease incitement against Israel, security forces have taken the approach that economic stability and better quality of life in the West Bank contribute to calm tensions and reduce violence. This means that Israel does not have a clear overall strategy for enhancing the Palestinian economy but rather promotes narrow steps that contribute to economic stability and growth, such as increasing the number of work permits, expanding "door to door" movement of goods, promoting industrial zones, and so forth. These actions help maintain the West Bank's economic advantage over the Gaza Strip, contribute to the population's quality of life, and allow PA governmental mechanisms to function, but they do not add up to a major economic improvement or political resolution. Both Israel and the PA try to minimize the visibility of these moves for political reasons and continue hostile rhetoric toward one another. For example, Prime Minister Shtayyeh accused Israel of deliberately infecting Palestinian laborers with the coronavirus, while in reality the two sides coordinate on health matters closely and Israel has supplied the PA with medical equipment.

That said, the coronavirus tested the PA as to its governance capacity, and it passed with high marks. While Israel was dealing with the outbreak and its implications for the local economy, the PA's independent conduct prevented a humanitarian disaster that would not have been limited to its territory for long; its rapid and efficient conduct in the face of the pandemic helped contain the virus and prevent a loss of control. Cooperation with Israel had an important role in this public health achievement, but the PA spearheaded the

effort. The pandemic proved that the PA's ability to function effectively during a crisis is essential for Israel's national security and has importance in all political-security scenarios.

This conduct by the PA should strengthen the understanding in the Israeli government that the PA is an essential partner for regional stability, and that its independent functioning and prosperity are important to Israel's security, including containing the strength of Hamas. The Israeli government should thus refrain from moves that weaken the PA. This means first and foremost refraining from unilateral annexation, which would eliminate Israel-PA cooperation and ultimately threaten a collapse of the PA. Notwithstanding the sense of opportunity offered by the Trump plan and the focus of international attention on COVID-19 and the ensuing global economic crisis, the collapse of the PA would severely threaten Israel's security. The new government ought to try and jumpstart a political process with the Palestinians, based on phased transitional arrangements, which would allow the future creation of two separate and distinct states. Israel's encouragement and assistance toward the Palestinian economy would be an incentive for the PA and PLO leaderships to join negotiations toward a political framework.

From here emerge the following recommendations:

1. The Israeli government should define the strengthening of the Palestinian economy in the West Bank as a strategic objective, with gradually decreased dependence on Israel and international aid. At the same time it should be made clear that this does not replace a future political agreement (i.e., not "economic peace").
2. An inter-ministry taskforce should be established that includes all relevant government parties from the security, civilian, and economic realms. This taskforce should formulate an overall plan for promoting economic growth in the West Bank, similar to the plan for the advancement of Arab residents of East Jerusalem already approved by the government.
3. Israel should approach donor countries, as well as other potential contributors in the Middle East, in a request to support moves to revitalize the Palestinian economy and influence the PA to implement reforms that will encourage growth.
4. Both health and security cooperation with the PA must be maintained.