SM/03/393

December 8, 2003

To: Members of the Executive Board

From: The Secretary

Subject: **Macroeconomic Developments, Outlook, and Reform in the West Bank and Gaza—Note by Fund Staff for the Ad-Hoc Liaison Committee (AHLC) Meeting on December 10, 2003**

Attached for the **information** of the Executive Directors is a note on macroeconomic developments, outlook, and reform in the West Bank and Gaza, which has been prepared by the Fund staff for the AHLC meeting to be held in Rome on December 10, 2003.

It is not intended to publish this paper on the Fund's external website.

Questions may be referred to Mr. Toujas-Bernaté (ext. 36936) and Ms. Beidas (ext. 38922) in MCD.

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INTERNATIONAL MONETARY FUND

MACROECONOMIC DEVELOPMENTS, OUTLOOK, AND REFORM IN THE WEST BANK AND GAZA[1]

A. Macroeconomic and Fiscal Developments in 2003

Macroeconomic developments

Following two years of steep decline, the first half of 2003 showed signs that the Palestinian economy had stabilized and recovered slightly from its low point. The good harvest, recovery in the number of Palestinian workers in Israel, significant fall in the rate of unemployment, reports by businessmen and bankers, and recovery in the index of the Palestinian Securities Exchange since March, all point to a modest pick up in economic activity. But the Palestinian economy remains depressed and real GDP could still be some 30 percent below its level in 1999. Whether the modest recovery in the first half of 2003 will be reversed by the continuous conflict and associated curfews and closures remains to be assessed.[2] Accordingly, the estimates prepared in collaboration with the Palestinian authorities and the World Bank suggest that real GDP could grow by 4.5 percent in 2003, a modest increase after the 15 percent decline in 2002.[3]

The moderately positive development s in 2003, compared to 2002, are mainly the result of three factors: (i) an increase in residential construction driven by pent up demand in 2001 and 2002, leading to higher economic activity and employment; (ii) a gradual improved access to the Israeli labor market during the first nine months of 2003; and (iii) the return of a significant portion of the stock of withheld clearance revenues by the government of Israel. The latter permitted repayment of nearly all arrears owed by the Palestinian Authority (PA) to the private sector by end-August 2003, which provided a boost to Palestinian domestic demand. Real growth has also been driven by a large injection of private investment, spurred on by construction activity, and some growth in exports. Exports, however, still remain significantly lower than their pre-Intifada levels, reflecting the costly nature of restrictions and closures.

[1] Note by the International Monetary Fund to be presented to the AHLC Meeting in Rome on December 10, 2003.

[2] "Closure" is the summary term for the imposition of restrictions on the movement of Palestinian goods and people across borders and within the West Bank and Gaza. Closures are viewed as essential by the Government of Israel to protect its citizens from violence.

[3] This estimate will likely be revised in view of economic and employment indicators for the full year.

Inflation in the West Bank and Gaza continues to be entwined with inflation in Israel, its biggest trading partner. Following monetary tightening by the Bank of Israel, some retrenchment in fiscal policy in Israel, and a resulting appreciation of the shekel, inflation is projected to decline from about 6 percent in 2002 to only 1 percent in 2003.

Another positive development was the significant reduction in the level of unemployment from 31 percent in 2002 to 24 percent in the third quarter of 2003. The reduced unemployment level is attributable to higher domestic employment, particularly in the private sector, which in the third quarter of 2003 surpassed the pre-Intifada levels and a larger number of Palestinian workers in Israel compared with last year. The employment rise in the period after mid-2002 was broad based, extending across many sectors. The unemployment rate, however, remains considerably higher than the pre-Intifada level of 10 percent. Labor supply will continue to grow rapidly, exceeding the 4 percent annual growth in the working-age population since the participation rate is likely to recover from the low levels of 2002.

Despite the poor economic environment, the banking sector as a whole remains in a reasonable shape and is undergoing some consolidation. Bank deposits have remained fairly stable and the largest bank had extended some new loans in the first half of 2003 (a significant change from the very conservative lending policies of banks since the beginning of the Intifada). The proportion of nonperforming loans has fallen from 29 percent in the fourth quarter of 2002 to 26 percent in the second quarter of 2003. Another positive indicator is the increase in the volume of checks presented for clearing, which is well above the mid-2002 level.

Budgetary developments in 2003

The fiscal situation in the West Bank and Gaza continues to be difficult despite some very positive developments that have taken place since the beginning of the year.

Total budgetary revenue has been remarkably strong since the beginning of the year, and became even stronger in the last few months, when it reached a level only 20 percent lower than before the beginning of the Intifada. Overall, it is expected that actual PA revenues in 2003 will exceed budget estimates by about US$120 million. Several factors accounted for this improvement. First, since their resumption in December 2002, the net regular monthly flows of clearance revenues from Israel have been steadily improving. Second, domestic revenue directly collected by the PA was above budget expectations, benefiting from transfers to the budget from the PA's commercial activities under the Palestinian Investment Fund (PIF) in April and October of a total amount of US$24 million. The stronger-than-expected collection of revenues was mainly the result of improvements in tax administration and a major collection effort, despite the difficult situation on the ground. In addition, the takeover of the Petroleum Commission, coupled with a change in management and pricing policy, resulted in higher sales of petroleum products and sharp increases of excise revenues in July–October 2003 (by about US$5 million per month).[4] Higher budgetary revenue is also consistent with signs that economic activity has slightly improved since the beginning of the year.

The strong revenue performance did not trigger, however, an expansion in expenditure. Rather, expenditures (excluding donor-financed capital expenditures and net lending) were broadly as envisaged in the budget. This overall neutral expenditure stance was not uniform over the first nine months or across expenditure categories. Reflecting a progressive increase in public employment, a salary increase for security personnel (of 8 percent effective June 1) and civil servants as a result of the partial implementation of the 1998 civil service law (see below), and the appreciation of the shekel against the dollar, the wage bill increased from US$55 million in January to US$65 million in October, exceeding the level envisaged in the budget. Indeed, civil service employment increased between December 2002 and September 2003 by 2,108 employees, still below the increase envisaged for 2003 in the revised budget (2,771 employees), 60 percent of which were in social sectors. In addition, security employment increased by 3,057 during the same period, leading to a security wage bill exceeding the budgetary appropriation.[5]

However, nonwage expenditures were squeezed by a monthly average of US$9 million below budget. This cut in nonwage expenditure was more pronounced in the first quarter in anticipation of a shortfall in financing, but then began to ease after April. This cautious easing was necessary in order to ensure a continued smooth functioning of the public administration and services. In addition to these budgeted expenditures, the PA was obliged to repay bills on behalf of municipalities owed to Israeli companies.[6] These payments, which municipalities agreed to reimburse in the future, averaged US$16 million per month, and were deducted from the gross transfers by Israel out of the stock of tax revenues withheld in 2001–02, as well as from monthly clearance revenues for water bills. Toward the end of the third quarter there was a further tightening of nonwage expenditure due to a sharp decline in budget support.

Even with the stronger than expected revenue performance and the neutral expenditure stance, the overall fiscal situation remained very tight because of a significant shortfall in external budget support. The low level of budget support stems mainly from shortfalls by Arab League donors (US$12 million vs. US$30 million per month in the budget assumption) and new procedures attached to the EU's assistance, which totaled only US$20 million during the first nine months while the budget envisaged monthly support of US$10 million.

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[4] Excise taxes on petroleum products are part of clearance revenues.

[5] The 2003 security wage bill is projected at US$287 million compared with a budget appropriation of US$271 million at the 2003 average exchange rate.

[6] Shown as "net lending" in Table 4.

The six-month extension of the Arab League budget support decided in March 2003 expired in September and no formal renewal has been extended. Out of the first disbursement of US$45 million from the EU to a special treasury sub-account from a new financing facility agreed with the PA in June, US$6 million has been released to the treasury and another US$30 million is expected to be disbursed before year's end. Despite a US$20 million disbursement from the United States in July, total external budget support during January-October was less than half of what was expected in the budget (US$21 million a month).

In spite of these developments, the Ministry of Finance (MOF) made good progress toward the objective of reducing the stock of budgetary arrears. As outlined in the budget, the MOF used the transfers from the accumulated stock of withheld tax revenue by Israel (net of the deductions made for the repayments on behalf of Palestinian municipalities) to repay arrears to the private sector of about US$130 million, which helped the private sector recover somewhat from the liquidity squeeze it experienced in the last three years. The transfers of withheld tax revenue have been indeed steady as expected for the first seven months of the year but were then brought to an abrupt stop due to withholding of NIS832 million by order of Israeli courts' pending resolution of claims against the PA by private Israeli companies. These transfers amounted to a net sum of NIS100 million (about US$20 million) monthly from January to May and NIS150 million (about US$30 million) in June and July. Consequently, while the budget expected transfers of accumulated tax revenue to amount to US$40 million per month, the actual amount received averaged US$17 million.

In view of the shortfall in budget support, the MOF had to increase its indebtedness to the banking sector by US$34 million by end-October, bringing the stock of debt to banks to a relatively high level of US$147 million (4.5 percent of GDP). Also, while substantial arrears were repaid to the private sector, new arrears were accumulated on the pension contributions to the GPIC, as well as other public sector arrears, amounting to a total of US$57 million during the first ten months of the year. Assuming that no new arrears would be accumulated until the end of the year, the net overall repayment of arrears in 2003 is expected to amount to US$72 million, leaving a total stock of arrears of about US$340 million at end-2003.

The last two months of the year will likely feature further squeezing of nonwage expenditure to accommodate the civil service wage increase and a further increase in the PA's indebtedness toward the banking sector, instead of lowering it as foreseen in the budget. The wage bill for the last two months is expected to average about US$71 million per month, reflecting the first round of a full civil service salary increase, as envisaged in the civil service law. This began with the Ministry of Education (on September 1), and was followed by the PCBS, Women's Affairs, Cabinet Office and Information (on October 1), with the remainder of the civil service to be covered by year end. If additional external budget support is not disbursed, it is possible that the PA would incur new arrears.

Reforms achieved between March and December 2003

Significant progress in establishing a transparent and strong revenue and expenditure system, and improving financial control were achieved since the last AHLC meeting in March. Most notably the MOF initiated a reform of the largest monopoly, petroleum, contributing to stronger revenues as well as improved market efficiency, as demonstrated by recent sales and excise revenue increases. In addition, the plan to retire civil servants at the age of 60 is being implemented, and a National Pension Committee was appointed recently by the cabinet to begin deliberations on a pension law (see Box 1). These reforms have placed the PA at a level of fiscal responsibility, control, and transparency, which is among the best in the region.

Box 1. Public Finance Reforms Achieved Since March 2003

On the revenue side

- All revenue continues to be channeled to the Single Treasury Account (STA), which is functioning very well. In addition to domestic revenue and transfers of tax revenue collected by Israel, the STA also received most external budgetary aid, including from Arab countries and the EU.
- PA assets consolidated under the Palestinian Investment Fund (PIF) are being audited and available on the PIF website.[7] In this context, an important development since March has been the transfer to the STA of PA companies' profits in both April and October 2003.
- The MOF initiated a reform of the largest monopoly, petroleum, contributing to stronger revenues as well as improved market efficiency, as demonstrated by recent sales and excise revenue increases. Until this year, the petroleum commission had an inappropriate pricing policy which resulted in loss of market share. Excise revenues were transferred to the budget but without transparency or accountability which may have led to some loss of revenue. This practice was discontinued after the Ministry of Finance took over the petroleum commission with the objective of turning it into a regulatory agency and privatizing its commercial operations.
- In addition to these reforms, administrative efforts have been taken to strengthen revenue collection (e.g. improved invoice system).

On the expenditure side

- Measures have been taken to improve transparency in salary payments and an audit of payroll has been initiated. All civil servants and about 25,000 (out of a total of 56,600) security personnel now receive their salaries by direct bank deposit controlled by the payroll at the MOF. Remaining security personnel are expected to adhere to this system before year-end. Salary deductions and the 6 ½ percent emergency tax (to fund payments to the unemployed and job creation) were abolished, resulting in a loss of revenue to the treasury of about US$24 million in 2003 or US$49 million on a yearly basis.

[7] www.pa-inv-fund.com/lasse.asp

- The MOF submitted to the PLC two quarterly budget execution reports this year and shifted to monthly reporting (see below) on its web site.
- The plan to retire civil servants at the age of 60 is being implemented, while MOF resumed its pension contributions to the Gaza Pension Fund (thus freezing the growth in pension arrears). In addition, a National Pension Committee was appointed recently by the cabinet to begin deliberations on a pension law expected in 2004.
- The long awaited civil service law (adopted in 1998), began to be implemented, entailing job regrading from a previous scale of 1–12 to 1–8, raising the minimum wage from NIS700 per month to NIS1000. Once the full impact of the first round of salary adjustments occurs, the civil service wage bill is expected to increase by 15 percent.

In the area of control and improved transparency

- Internal audit procedures were issued (with a new charter) and auditors are being trained and deployed at various ministries and agencies to conduct post payment audits. An auditing system is also being established for PA revenues, payroll, and purchasing.
- Fiscal data availability was improved through the publication by the Ministry of Finance on its web site on a monthly basis of detailed government revenue and expenditure data within a week's lag since September.[8] This is among best practices in the region, and was made possible after the unification of the accounting system, through a common budget classification and networked computer system in between West Bank and Gaza and a unified chart of accounts, thus consolidating expenditure management.

B. Outlook for 2004

Macroeconomic outlook

Given the centrality of the political developments in the West Bank and Gaza, the economic outlook for 2004 critically depends on the key assumptions made concerning any political progress. The uncertainty that necessarily surrounds any prediction can hardly be overstated. Nevertheless, three scenarios have been developed to capture the salient features of the economy in the different states.

The baseline scenario assumes a status quo: the persistence of the current political instability and vulnerability are assumed, reflected in a continuation of current levels of internal and external movement restrictions on persons and goods, and transaction costs similar to those of today.

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[8] www.mof.gov.ps/reports.htm

Under this scenario, there would be some deceleration in the growth rate to 3.5 percent as the initial boost to the domestic economy from residential construction subsides. Unemployment is projected to decline slightly on account of higher private and public employment within the WBG. Higher public spending is expected through an increase in the wage bill and to meet the growing population's need for public services, thus stimulating aggregate demand. However, private investment is expected to remain largely unaltered after the rebound of 2003.

Two other scenarios have been developed. The first assumes some political progress with the road map, as shown by respective parties' implementation of commitments under Phase I and Phase II of the road map. In this case, there would be considerable improvements in the economic situation stimulated by greater worker remittances and fewer restrictions on movement of goods and people. Consequently, real growth could reach 9 percent in 2004. The second scenario assumes some political deterioration, marked by increased external and internal movement restrictions which would prove costly to the Palestinian economy resulting in a decline in GDP by about 5 percent in 2004.

The 2004 budget

The budgetary outlook, as presented below, is based on the baseline scenario. It is assumed that the strong trend in revenue of the last few months would continue, raising the ratio of total revenue to GDP from 22 to 25 percent in 2004. This is driven by the full-year impact of an increase in revenues associated with improvements in tax administration and the efficiency and liberalization gains in the petroleum market. Nevertheless, revenues will remain below their "normal" level because of the economic downturn.[9]

Recurrent expenditure is expected to rise faster than the improved revenue performance on several accounts, from 35 to 40 percent of GDP. First, the wage bill share of GDP would rise from 23 to 25 percent in 2004, reflecting the carry-over of the salary increase for all civil servants, which took effect in the last quarter of 2003, and a 3,500 increase in civil service employment.[10] Second, and following their squeeze during 2003, nonwage expenditure should recover substantially above the 2003 budget level, in order to cover pressing and growing needs for operations and maintenance as well as public services for a rapidly growing population and in the context of a severe dislocation resulting from the Israeli separation fence and closures. Third, transfer payments would increase in line with the wage bill to reflect higher social contributions, and there will be additional costs associated with establishing a secretariat for the Prime Minister's office, a new ministry for women's affairs and holding elections in June 2004, for which US$15 million have been budgeted.

[9] Defined as the 1999 revenue level adjusted for an average growth rate in line with population growth.

[10] The first round increase in salaries for the whole civil service is estimated to raise average salaries by about 15 percent. A second round envisaged in the Civil Service Law may not be carried out in 2004 because of budget constraints.

To fully cover the budget deficit, the PA would need about US$650 million of external budget support. This would obviously require a special effort on the part of donors, as this amount is more than double that expected to be disbursed in 2003.[11] The PA's indebtedness to the banking system has been relatively high in 2003 and should be reduced in 2004. The reduction is budgeted at US$12 million. The large stock of arrears should also be progressively repaid. To this end, any additional transfer of withheld tax revenues by Israel would be used to reduce the stock of domestic arrears should revenues increase beyond the budgeted amount, the MOF intends to have a further reduction in indebtedness to the banking system and/or in the stock of arrears.

Unless the assumptions of this baseline scenario are improved, leading to a significant reduction in internal and external movement restrictions and associated transactions costs, the main conclusion stemming from the 2004 budget is that the PA can not cover the wage bill for 2004 through projected tax revenues. The wage bill will indeed represent about two-thirds of total current expenditure, leaving limited room for maneuver in expenditure management. Therefore, the PA will remain dependent on external financing to balance the recurrent budget until such time when economic activity regains its normal pace.

Budget support in 2004

Previous studies comparing budget support to other forms of donor assistance concluded that it was the most efficient method of sustaining employment and stimulating the economy of the West Bank and Gaza, including through the support it provides to the private sector by sustaining demand for domestic products. A recent World Bank study[12] argued that the multiplier effects of salaries, which have been financed partially by budget support, exceeded those associated with other types of expenditures i.e. a dollar disbursed against salaries was allocated to a basket of goods and services with higher domestic content than a dollar disbursed against other expenditures. In this context, the macro benefits of budget support were clear given that this donor money would not have been available otherwise. In addition, welfare benefits were significant since PA employment of about 130,000 supported a minimum of 840,000 people. The study argued that canceling budget support would push at least another 100,000 people into poverty. An additional benefit to budget support if channeled through the STA, is that it is simple to administer, with minimal overhead costs, and supports transparency in public finances without raising the issue of fungibility. On this

[11] The only other possible source of financing is the expectation that the transfer of US$180 million of withheld tax revenues by Israel stopped in September 2003 pending the resolution of cases brought to Israeli courts would be resolved. However, as shown in the 2004 budget, these revenues would be entirely used to further reduce the stock of domestic arrears. Based on recent court decisions, there are however serious doubts that this source of financing would be forthcoming in 2004.

[12] Twenty Seven Months—Intifada, Closures and Palestinian Economic Crisis: An Assessment, World Bank, May 2003.

basis, this form of assistance should be given top priority in any external financing support that donors may consider.

Reforms envisaged in 2004

The 2004 budget is underpinned by a number of policy reforms. On the revenue side, the submission of a new income tax law to the Palestinian Legislative Council (PLC) based on international best practice will be more favorable to private sector activity while raising overall revenue. On the expenditure side, the consolidation of all security personnel under one supervisory authority with their wages paid by direct bank transfer will allow for improved transparency and control over hiring. In addition, following the rise in civil service employment in 2003, MOF intends not to fill positions which became vacant so that the increase in the 2004 budget would be limited to 1,000–2,000 (rather than 3,500) positions, with the majority of the increase applied to health, education and judiciary services. In this context, the MOF will continue to retire civil servants at the age of 60, which should also reduce net hirings. Finally, to alleviate the moral hazard stemming from payments of municipalities' utility bills by the PA, net lending to municipalities should fall from US$187 million to US$120 million as they begin to make some payments and collect some fees, under a strict payment plan worked out with them to ensure that they meet a budget constraint.

Further expected progress in other reforms in 2004 includes ongoing work, in collaboration with the World Bank, on setting new parameters of the pension system, on which a decision is expected in early 2004. A new pension law could then be adopted by mid-2004. Pension reform should provide a unified, fully funded, and sustainable pension system. The lack of such a pension system has been a major impediment to civil service reform and security organizations' retrenchment. The pension reform will therefore be key in efforts to curb the rising trend of the wage bill in the near future. In addition, auditing of existing pension arrears is expected to be completed. Second, compliance with the basic law in the area of public procurement, particularly security, should be handled competitively and transparently. Third, the results of the civil service payroll audit are expected. Fourth, the valuation and audit of all PA assets should be completed and published, and an assessment of the transfers of profits to the budget made. Fifth, the finalization of the 2002 fiscal operations are expected by year's end. Sixth, external auditing procedures should be strengthened through the drafting of a new external auditing law to ensure full independence of the office, submission of regular reports to the PLC, and comprehensive coverage of all PA institutions. This would address concerns regarding the independence and mandate of external auditors. Finally, a clear and sustainable financial relation with municipalities (local government) should be established. These are currently experiencing a very low payment rate for utility bills by the public, which prevents them from paying their bills to energy producers, in particular to Israeli companies.

Many of these reforms will need to be encouraged and supported by donors, including for some through continued technical and higher budget support and other financial assistance.

Table 1. West Bank and Gaza: Macroeconomic Framework, 1997–2004

	1997	1998	1999	2000	2001	2002	2003	2004
Output, employment and growth rates								
Real GDP growth (in percent)	12.2	11.8	8.9	-5.4	-15.0	-14.5	4.5	3.5
Real GNI growth (in percent)	12.4	16.3	8.4	-6.8	-16.2	-16.4	5.7	1.4
Nominal GDP (in millions of U.S. dollars)	4,009	4,258	4,517	4,442	3,765	2,975	3,260	3,264
Nominal GNI (in millions of U.S. dollars)	4,661	5,159	5,454	5,274	4,398	3,404	3,776	3,709
Per capita nominal GDP (U.S. dollars)	1,441	1,469	1,496	1,410	1,141	859	897	859
Per capita nominal GNI (U.S. dollars)	1,675	1,781	1,806	1,674	1,333	983	1,039	976
Per capita nominal GNI (NIS)	5,776	6,767	7,477	6,827	5,607	4,657	4,748	4,589
growth rate	12.1	17.1	10.5	-8.7	-17.9	-16.9	2.0	-3.3
Nominal gross domestic investment								
Government (in millions of U.S. dollars)	262	272	318	242	229	204	263	268
growth rate	8.3	3.6	16.9	-23.8	-5.4	-10.8	28.9	1.9
Private and other (in millions of U.S. dollars)	1,005	1,112	1,408	1,117	745	382	475	483
growth rate	5.0	10.6	26.6	-20.6	-33.3	-48.7	24.2	1.7
Unemployment (% of total labor force)	20.3	14.4	11.8	14.1	25.5	31.3	26.0	29.0
Employment (in '000)	480	548	588	597	508	486	581	573
o.w. in Israel	82	119	135	117	70	50	57	50
o.w. in West Bank and Gaza	398	429	453	480	438	436	524	523
o.w. civil service 1/	81	91	104	115	122	125	130	134
growth rate	16.4	11.9	14.3	11.0	6.3	2.2	4.4	2.7
o.w. private sector 2/	317	338	350	365	316	311	394	389
growth rate	6.4	6.8	3.4	4.4	-13.5	-1.6	26.6	-1.3
Consumer price index 3/	7.6	5.6	5.5	2.8	1.2	5.7	1.1	0.2
Fiscal operations				(In percent of GDP)				
Revenue 4/	20.6	20.3	22.1	21.4	7.2	10.1	21.5	24.4
Recurrent expenditures 5/	21.6	19.8	20.9	26.9	29.1	33.6	35.0	40.0
Total expenditures 6/	28.2	26.1	27.7	32.3	34.6	40.4	42.8	47.7
Recurrent balance	-1.1	0.5	1.2	-5.5	-21.9	-23.6	-13.5	-15.7
Overall balance 5/	-7.6	-5.9	-5.6	-10.9	-27.3	-30.3	-21.3	-23.3
Budget support	...	...	...	1.2	14.1	15.7	11.5	12.6
Current account (including transfers)				(In millions of U.S. dollars)				
Exports of goods and non factor services	767	887	892	867	535	413	448	466
Imports of goods and non factor services	3028	3320	3805	3404	3221	2765	2933	2879
Net factor income	651	902	937	833	633	430	516	445
Net transfers	470	410	399	586	1173	1757	1516	1346
Current account balance	-1140	-1121	-1577	-1118	-881	-165	-453	-623
Money and Banking				(In millions of U.S. dollars)				
Deposits 7/	1890	2249	2671	3338	3222	3078	3329	3333
Growth rate	14.9	19.0	18.8	24.9	-3.5	-4.5	8.2	0.1
Demand deposits 7/	562	615	686	815	761	780	985	986
Time deposits 7/	1329	1635	1985	2522	2461	2298	2344	2347
Claims to the private sector 7/	563	733	913	927	860	859	848	849
Growth rate	37.8	30.2	24.4	1.6	-7.2	-0.1	-1.3	0.1
Memorandum items:								
Population growth (percent)	5.8	4.1	4.2	4.3	4.7	5.0	4.9	4.5
Average NIS/US$	3.45	3.80	4.14	4.08	4.21	4.74	4.57	4.70

1/ PA employment only, end of period.
2/ includes local governments and public enterprises.
3/ Percentage change of CPI over previous year
4/ excludes accrued clearance revenue not transferred by Israel in 2001 and 2002 and transfers from accumulated stock in 2003 and 2004.
5/ excludes net lending.
6/ includes PA and donor financed capital expenditure.
7/ end of period.

Table 2. West Bank and Gaza: National Accounts

12/2/2003 16:32	1997	1998	1999	2000	2001	2002	2003	2004
Real GDP growth rate	12.2	11.8	8.9	-5.4	-15.0	-14.5	4.5	3.5
				Composition of Real GDP growth				
				In million US$ (1997 constant prices)				
Composition of real GDP growth	4012	4486	4883	4619	3927	3358	3509	3629
Imports of goods and services	3015	3428	4082	3514	3419	3056	3099	3085
Exports of goods and services	767	920	954	889	554	450	468	496
Consumption	4906	5399	5849	5736	5680	5277	5314	5354
Private	4043	4420	4787	4574	4552	4178	4121	3951
Public	863	980	1062	1162	1128	1099	1193	1403
Gross Fixed Investment	1267	1501	2010	1467	1072	688	826	863
Private	1005	1206	1640	1206	820	449	532	555
Public	262	295	370	261	252	239	294	308
Change in inventories	86	94	152	40	40	0	0	2
Net errors and omissions	12	16	13	8	10	11	11	11
Net factor income from abroad	651	939	1000	863	668	484	554	490
of which: labor income from Israel	560	896	947	813	495	399	465	408
of which: investment income	91	43	53	50	173	85	89	83
Gross National Income (GNI)	4663	5425	5883	5482	4595	3843	4063	4119
Net current transfers	470	427	425	607	1239	1979	1629	1484
Gross National Disposable Income (GDI)	5133	5852	6308	6090	5834	5822	5692	5603
				(annual change in percent of previous year)				
Composition of real GDP growth	12.2	11.8	8.9	-5.4	-15.0	-14.5	4.5	3.4
Imports of goods and services	7.0	13.7	19.1	-13.9	-2.7	-10.6	1.4	-0.4
Exports of goods and services	5.2	19.8	3.7	-6.8	-37.6	-18.9	4.0	6.0
Consumption	9.6	10.0	8.3	-1.9	-1.0	-7.1	0.7	0.7
Private	9.6	9.3	8.3	-4.4	-0.5	-8.2	-1.4	-4.1
Public	9.8	13.5	8.4	9.4	-3.0	-2.6	8.6	17.6
Gross Fixed Investment	12.2	18.5	33.9	-27.0	-26.9	-35.8	20.1	4.4
Private	11.5	20.1	36.0	-26.5	-32.0	-45.3	18.5	4.4
Public	15.0	12.4	25.5	-29.4	-3.6	-4.9	23.0	4.6
Net factor income from abroad	14.1	44.2	6.5	-13.6	-22.6	-27.6	14.5	-11.5
of which: labor income from Israel	15.7	60.0	5.6	-14.1	-39.1	-19.4	16.5	-12.3
of which: investment income	5.0	-53.1	23.6	-5.7	248.2	-50.8	4.9	-7.6
Gross National Income (GNI)	12.4	16.3	8.4	-6.8	-16.2	-16.4	5.7	1.4
Net current transfers	-6.6	-9.0	-0.5	42.8	104.0	59.8	-17.7	-8.9
Main assumptions								
No. of Palestinian workers in Israel (basis for GNI)	82,045	118,881	135,000	117,000	70,000	50,000	57,000	50,000
Alpha: Average propensity to import (w.r.t. GNI)	0.60	0.60	0.66	0.59	0.60	0.60	0.61	0.63
Beta: Average propensity to consume (w.r.t. GNI)	0.85	0.82	0.83	0.81	0.85	0.85	0.84	0.84
Tau : Effective tax rate for domestic tax (w.r.t GDP)	0.08	0.08	0.08	0.08	0.07	0.08	0.08	0.08

Table 3: West Bank and Gaza: Fiscal Developments in 2003
(In millions of U.S. dollars, unless otherwise stated)

	MonthlyBudget @ 5.00	MonthlyBudget @ 4.56	Actual Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sept.	Oct.	Avr. Jan-Oct	Total Jan-Oct
Revenue	44.3	48.6	49.9	55.5	55.2	62.9	48.8	47.5	69.4	70.9	67.4	71.0	59.9	599
Domestic	17.3	19.0	17.6	15.1	20.3	35.9	12.9	19.1	26.6	21.2	19.3	24.8	21.3	213
Gross monthly clearance 1/	27.0	29.7	32.3	40.4	34.9	27.1	35.9	28.5	42.7	49.7	48.0	46.2	38.6	386
Expenditure	87.0	95.6	62.8	70.2	78.3	85.8	94.6	94.5	105.9	106.1	106.5	100.0	90.5	905
Gross wages	53.0	58.2	55.2	54.3	55.4	57.3	59.8	63.0	63.0	63.0	65.9	65.7	60.3	603
Non-wage expenditure	34.0	37.4	7.7	15.8	21.9	27.8	33.3	30.2	40.3	38.5	34.7	29.0	27.9	279
PA financed capital spending	1.8	2.0	0.0	0.0	1.0	0.8	1.5	1.3	2.6	4.5	5.9	5.2	2.3	23
Net lending 2/	0.0	0.0	1.9	55.5	1.7	15.1	36.9	5.7	2.2	27.9	2.5	6.2	15.6	156
Balance	-62.3	-68.4	-14.9	-70.1	-24.7	-38.0	-82.7	-52.7	-38.7	-63.1	-41.7	-35.1	-46.2	-462
External budget support	44.6	49.0	17.6	26.0	21.7	19.6	30.4	4.7	50.8	2.2	24.9	8.3	20.6	206
Balance including budget support	-17.7	-19.4	2.7	-44.2	-3.0	-18.3	-52.3	-48.0	12.0	-60.8	-16.8	-26.8	-25.6	-256
Total other financing	17.7	19.4	-2.7	44.2	3.0	18.3	52.3	48.0	-12.0	60.8	16.8	26.8	25.6	256
Gross withheld clearance revenues 3/	40.0	43.9	21.0	72.4	20.8	34.4	50.8	34.2	34.3	25.7	0.0	0.0	29.4	294
Net arrear accumulation	-34.6	-38.0	-11.8	-54.7	-30.5	-30.5	-13.4	49.4	-15.4	36.8	-2.5	0.4	-7.2	-72
Net domestic bank financing	-5.4	-6.0	-11.8	26.5	12.7	14.5	14.8	-35.7	-31.0	-1.7	19.3	26.4	3.4	34
Memorandum items														
Exchange rate NIS/$	5.00	4.55	4.76	4.81	4.80	4.64	4.49	4.38	4.37	4.45	4.46	4.45	4.56	4.56
PA Employment	...		122,779	124,056	125,549	126,010	126,367	127,382	127,045	127,169	127,493	127,067	-	127,067
o.w. civilian	72,929		70,631	71,598	72,330	72,729	72,755	72,932	72,440	72,260	72,264	71,734	-	71,734
o.w. security	...		52,148	52,458	53,219	53,281	53,612	54,450	54,605	54,909	55,229	55,333	-	55,333

Sources: Ministry of Finance; and IMF estimates

1/ Includes payments deducted for dues owed to the Israeli water company Mekorot, while the budget figure is on a net basis.

2/ Payments deducted at source by GOI from disbursements of withheld clearance revenue for owed bills by Palestinian municipalities.

3/ Monthly figures include deductions by GOI for utility bills, while the budget figure is on a net basis.

Table 4: West Bank and Gaza: Fiscal Developments in 2002–05
(In millions of U.S. dollars, unless otherwise stated)

	2002	2003		2004
	Actual	Budget	Proj.	Budget
Revenue	254	583	700.4	806
Domestic	225	227	259	246
Gross monthly clearance 1/	29	356	442	560
Current Expenditure	1,016	1147	1140	1306
Gross wages	676	699	736	828
Non-wage expenditure	340	448	404	478
Capital expenditure	211	257	263	268
PA financed	11	24	7	18
Donor financed 2/	200	233	256	250
Net lending 3/	0	0	187	120
Balance	-973	-821	-889	-888
External budget support	467	588	250	0
Balance including budget support	-506	-233	-640	-888
Total financing	506	233	516	-12
Donor financed capital spending 2/	200	233	256	0
Gross withheld clearance revenues 4/	46	527	294	180
Net arrear accumulation	111	-456	-72	-180
Net domestic bank financing	149	-71	38	-12
Financing gap	0	0	124	900
Budget support	0	0	124	650
Capital spending	0	0	0	250
Memorandum items				
Exchange rate NIS/$	4.74	4.56	4.55	4.70
PA Employment	124,817		128,262	
o.w. civilian	71,166	72,929	72,929	76,429
o.w. security	53,651	...	55,333	...

Sources: Ministry of Finance; and IMF estimates.

1/ Includes amounts deducted for dues owed to the Israeli water company Mekorot.

2/ Preliminary estimates.

3/ Payments deducted at source by GOI from disbursements of withheld clearance revenue for owed bills by Palestinian municipalities.

4/ Monthly figures include deductions by GOI for utility bills, while the budget figure is on a net basis.