

SM/07/333

September 20, 2007

To: Members of the Executive Board

From: The Secretary

Subject: **Macroeconomic and Fiscal Developments in the West Bank and Gaza—
Note by Fund Staff for the Ad-Hoc Liaison Committee (AHLC) Meeting
on September 24, 2007**

Attached for the **information** of Executive Directors is a note on macroeconomic and fiscal developments in the West Bank and Gaza, which has been prepared by the Fund staff for the AHLC meeting to be held in New York on Monday, September 24, 2007. At the time of circulation of this note to the Board, the Secretary's Department has received a communication from the authorities of the West Bank and Gaza indicating that they consent to the Fund's publication of this paper.

Questions may be referred to Mr. Kanaan, MCD (ext. 34001).

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**MACROECONOMIC AND FISCAL DEVELOPMENTS
IN THE WEST BANK AND GAZA**

AD HOC LIAISON COMMITTEE MEETING

NEW YORK, SEPTEMBER 24, 2007

INTERNATIONAL MONETARY FUND

**MACROECONOMIC AND FISCAL DEVELOPMENTS
IN THE WEST BANK AND GAZA**

I. RECENT ECONOMIC DEVELOPMENTS

1. **The Palestinian economy entered a very difficult phase following the formation of the Hamas-led government in early-2006.** Economic activity was curtailed by the intensified restrictions on movement and access, particularly across Gaza's borders. The situation was exacerbated by the destruction of physical infrastructure during the Israeli incursion into Gaza, the limited financing for government spending as a result of financial sanctions, and increased uncertainty about the Palestinian territories' prospects. Gross Domestic Product is estimated to have fallen by 5 to 10 percent in real terms in 2006, leaving average real GDP per capita almost 40 percent below its 1999 level. By comparison, real per capita GDP in Israel rose by almost 10 percent over the same period. Indicators of the labor market, trade with Israel, deposits with banks, and indirect tax revenues suggest that the pace of economic decline may have eased during the first half of 2007. However, the tightening of trade restrictions on Gaza since the Hamas takeover in June 2007 is likely to have further reduced economic activity in that area in the second half.

2. **The decline in economic activity has been particularly pronounced in Gaza, which has been subject to greater instability and tighter closures by Israel than the West Bank.** The unemployment rate was estimated at about 35 percent in Gaza and 20 percent in the West Bank in 2006. Poverty levels have been increasing, with some surveys indicating that about two-thirds of households in the West Bank and Gaza (WBG) were below the poverty line at end-2006.¹ The World Food Programme and the Food and Agriculture Organization have warned that rising unemployment and poverty are posing acute challenges to food security. The economic and humanitarian situation in Gaza has deteriorated markedly since the Hamas takeover, with the closure of the primary border crossings with Israel and the consequent drawdown of stocks of basic commodities.

3. **Unemployment remains high, but has declined slightly due to temporary factors.** According to the Palestinian Central Bureau of Statistics (PCBS), employment in WBG increased by 4 percent (31,000 workers) between the last quarter of 2006 and the second quarter of 2007, reaching a total of 749,000 workers. Almost all of this increase was concentrated in Gaza, largely reflecting temporary employment generation programs by UNRWA and increased Palestinian Authority (PA) employment. As a result, the overall

¹ According to the July 2007 report by the United Nations Development Programme (UNDP), a majority of Palestinians, about 58 percent, live below the poverty line, and about half of them (30 percent of the population) live in extreme poverty. A majority of Palestinians (about 60 percent) reported a decline in their household incomes in 2006–07.

unemployment rate stood at 19 percent in the second quarter of 2007 (16 percent in the West Bank and 26 percent in Gaza), down from 24 on average in 2006. By comparison, unemployment was just under 12 percent in 1999, before the start of the second Intifada.

4. **Inflation remains low, at about 1 percent in the year to July 2007.** Price increases in WBG largely mirror inflation developments in Israel, and have been dampened by the appreciation of the New Israeli Shekel (NIS) in 2006. While inflation has been tempered by the decline in Palestinian consumers' income, particularly in Gaza, prices continue to be buoyed by high transport costs due to restrictions on the movement of goods.

5. **Despite the difficult economic environment, banking sector deposits continued to grow,** increasing by about 11 percent in the year to June 2007. This reflected both continued growth in banking intermediation (the number of bank branches has increased by about 15 percent since end-2005) as well as strong inflows from the Palestinian diaspora. This has raised the deposits-to-GDP ratio to over 90 percent, which is high by regional standards. However, after expanding by about 8 percent in 2006, credit to the private sector remained stable during the first half of 2007, leaving the ratio of loans to deposits at a relatively low level. Banks were able to reduce their large exposure to the PA and its employees by liquidating collateralized assets and making regular deductions from salary payments.² Liquidity in the banking sector remains at about 75 percent in June 2007. Paid-up capital of banks has increased since 2005 by 75 percent, to about 8 percent of total bank assets. These indicators suggest that overall the banking sector is in a reasonably solid position to face potential borrowers' difficulties.

6. **The Palestinian Monetary Authority (PMA) has persevered in the implementation of strict prudential and regulatory standards in line with international practice.** It has worked closely with the Bank of Israel to ensure continued smooth relations between Israeli banks and those in the West Bank and Gaza in a difficult political environment. A new Anti-Money Laundering (AML) law was adopted by the PA government in August 2007, and will start being enforced in the coming weeks. New banking and PMA laws are in the final stage of preparation. Considerable progress continues to be made on internal reform and capacity building at the PMA with technical assistance from the IMF, the World Bank, and other TA providers.

II. FISCAL DEVELOPMENTS IN 2006 AND EARLY 2007

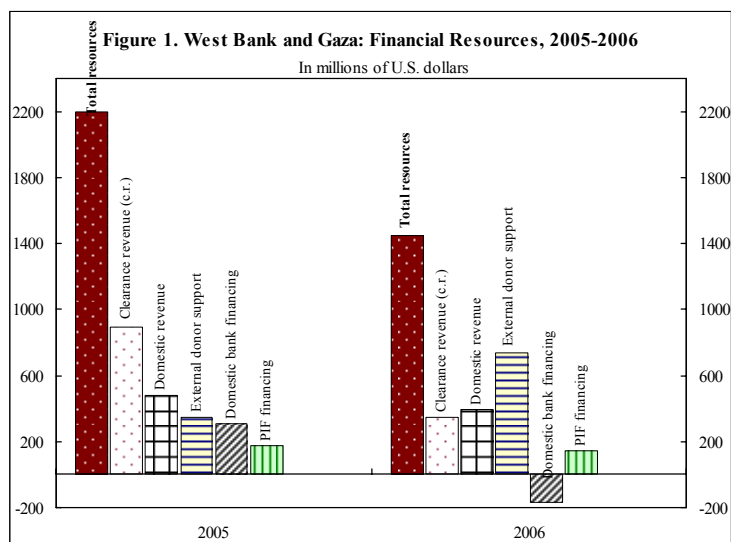
7. **The PA has been facing a severe liquidity crisis since early 2006.** It is estimated that, for 2006, budgetary resources fell by over a third compared to 2005 (from \$2.20 billion in 2005 to \$1.45 billion in 2006, see Tables 2 to 4), despite a doubling of external budgetary assistance, leading to a 30 percent contraction in cash spending. At the same time, expenditure

² The share of loans to the PA and its employees in total loans is estimated to have declined from above 45 percent in March 2006 to below 40 percent in June 2007.

commitments increased by 17 percent due to a rise in the wage bill, as well as in nonwage expenditure needed to meet the emergency needs of the population and the higher cost of energy and utilities. On a commitment basis, the fiscal deficit reached \$1.2 billion, or 26 percent of GDP. About \$0.9 billion in expenditure arrears were accumulated, owed to government employees, who received less than two-thirds of their regular salaries in 2006, as well as to the pension fund and to private sector suppliers.³

8. **The shortfall in resources was mainly the result of a sharp decline in the PA's revenues.** This reflected the withholding of clearance revenues by the Israeli government since March 2006. Out of an estimated \$770 million in clearance revenues collected by Israel, preliminary estimates suggest that only about \$344 million was available to fund government cash spending, directly or indirectly. In addition, only \$395 million in domestic tax and nontax revenues were collected in 2006, down from \$476 million in 2005. This was due largely to a drop in nontax revenues, as the Palestine Investment Fund (PIF) had paid exceptionally large returns to the budget in 2005. Domestic tax revenues remained at about the same level as in 2005, despite the decline in economic activity and weaker enforcement during government employees' strike in the latter part of the year. A significant part of tax revenue was withheld by banks to help cover the government's debt servicing obligations.

9. **While domestic financing was a major funding source in 2005, little could be mobilized in 2006.** The PIF continued to provide substantial financing—about \$150 million in 2006, thus continuing to draw down its assets—to help finance fuel imports and repay bank loans. However, banks sharply reduced their exposure to the PA, mainly for fear of possible legal repercussions. During 2006, the PA's net debt to commercial banks declined by about \$170 million. As a result, outstanding PA debt to commercial banks (including one bank abroad) fell to about \$500 million by end-2006.



10. **The decline in revenues and domestic financing was partly offset by a strong increase in external financing.** While most donors refrained from providing direct financial assistance to the PA government, they nonetheless continued to provide funds to support the

³ The total of \$0.9 billion includes about \$385 million in arrears on net wages (excluding those related to pensions and other wage deductions), \$175 million in arrears on pension contributions (employees' and government's contributions), and about \$200 million in arrears to the private sector (including Israeli suppliers and unpaid domestic tax refunds).

Palestinian people through a number of channels that bypassed the Hamas-led government. In fact, external financing to support recurrent budget operations reached about \$740 million in 2006, more than double the amount received in 2005 (see Table 5).⁴

11. **As resources fell sharply after the Hamas-led government took office, expenditures had to be prioritized.** Wages were accorded a high priority. However, while wages could still be paid in full in the first quarter, the wage bill could only be partly met in the remainder of the year. Overall, and including allowances paid by the Presidency and the European Commission's "Temporary International Mechanism" (TIM), government employees on average received payments equivalent to 60–65 percent of their normal wages in 2006. Operating expenditures and especially transfers were compressed in 2006. The PA government was able to pay neither the employers' contribution to the pension fund, nor the employees' contributions deducted from gross wages, further weakening the pension fund's already unsustainable financial position.

12. **Spending on energy and utilities continued to take up a disproportionate share of government spending.** Payments to cover the costs related to energy and utilities, including the subsidization of domestic petroleum products, amounted to about \$0.4 billion. This includes the amounts deducted from the clearance revenues withheld by Israel, including payments to the Israeli companies that provide utilities to the Palestinian territories. The deductions increased significantly since 2005, as collection rates for utilities declined. Spending on energy would have been even higher, had the Gaza power plant been fully operational throughout the year.

13. **The continued rise in the wage bill is particularly worrisome.** On a commitment basis and in local currency terms, it expanded by about 20 percent in 2006 compared with 2005. To a large extent, this reflects the full-year effect of the wage increases granted to both civil servants and security personnel in 2005, but it also reflects the continued expansion of the government payroll. Government employment, which had reached about 151,000 people at the end of 2005, rose further in 2006, to about 167,000 people (including an additional 12,500 security employees). With the steady appreciation of the Israeli currency, wages due reached almost \$1.2 billion in 2006 and averaged about \$108 million per month at the end of the year (compared to less than \$80 million per month prior to the wage increase in mid-2005), exceeding total revenues being collected, including those collected by the Government of Israel (GoI).

14. **Preliminary and partial data for 2007 so far indicate that the fiscal situation worsened further in the first half of this year.** Expenditure commitments continued to increase owing to: (i) the rise in the wage bill due to a surge in government employment (largely security personnel) in early 2007; and (ii) an increase in "net lending," due largely to a rise in the cost of energy and nonpayment of utility bills. At the same time, reflecting the worsening environment including the impact of the civil strife in Gaza, budgetary revenue is

⁴ That amount of external financing does not include additional amounts reported to have been received but not documented.

estimated to have declined in the first six months of 2007 compared to the same period last year. Clearance revenues collected by Israel continued to be largely withheld until July 2007.⁵ The shortfall in cash revenues was only partially offset by higher than expected external budgetary financing of about \$560 million.⁶ Thus a large part of the deficit continued to be financed through the accumulation of arrears on wages, pension fund contributions, and payment to private suppliers.

III. OUTLOOK FOR 2007 AND THE 2007 BUDGET

15. **The resumption of clearance revenue transfers in July 2007 has eased the liquidity situation and enabled the full payments of wages since then.** The total stock of clearance revenues collected between February 2006 and July 2007, net of deductions for payments of utilities and of transfers to the PA made during this period, is preliminarily estimated at NIS 2.7 billion (about \$650 million). Of that amount, almost NIS 400 million has been attached by Israeli courts. The GoI transferred a first installment of NIS 500 million in early July, and agreed to settle the full stock of withheld clearance revenue through monthly installments of NIS 370 million (about \$90 million). That stock is envisaged to be fully transferred by end-2007. Moreover, regular monthly transfers started again in early August.

16. **In mid-August 2007, the Cabinet approved the 2007 emergency budget, which will guide budget execution during September to December 2007.** Its broad aim is to make a start at setting public finances on a sustainable path and pave the way for a fiscal adjustment in 2008. In particular, the budget envisages a lowering of budgetary expenditure to around the level of cash resources (including the stock of withheld clearance revenue), so as to minimize further payment arrears accumulation in the remainder of 2007. Expenditure restraint would be achieved mainly through a strict government employment policy, based on the permanent retrenchment of 20,000 security employees effective in July 2007 (out of a total of 85,000 security employees, who constitute about half of total government employees).⁷ The budget also envisages the strengthening of the Public Financial Management (PFM) system in line with the recommendations of an IMF technical assistance mission, including the consolidation of banking arrangements and improvements in fiscal reporting.

⁵ GoI transferred \$100 million of clearance revenue to a PLO account in January 2007, following an agreement between President Abbas and Prime Minister Olmert in December 2006.

⁶ The total of \$560 million is about twice the level received in the same period last year, reflecting an exceptionally high contribution from Arab countries of about \$360 million

⁷ In late June 2007, about 31,500 PA employees were taken off the payroll pending a review of the legality of their status. This consisted of: (i) 23,500 security employees; and (ii) 8,000 civilian employees. The budget envisages that 20,000 out of the 23,000 security employees would be permanently retrenched, while the civilian employees would be reintegrated.

17. The 2007 emergency budget's underlying policy intentions and expectations can be summarized as follows:

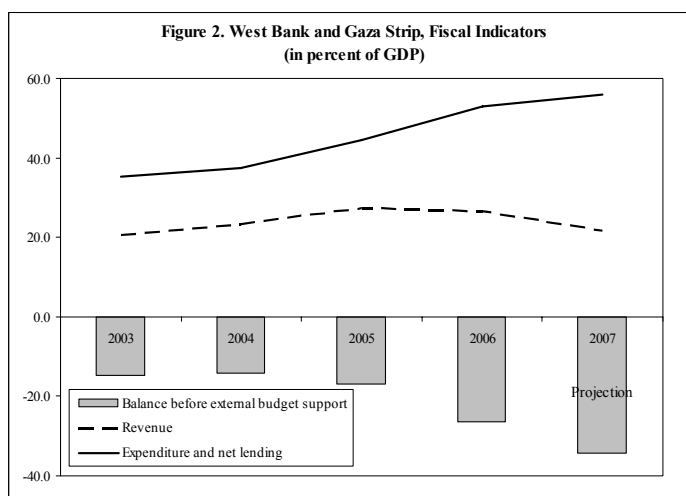
- A conservative outlook for budgetary revenue to reflect continued subdued economic activity, as well as the consequences of the events in Gaza, in particular the intensified restrictions on access and the fact that its domestic revenue is no longer remitted to the budget;⁸
- The transfer by the GoI of clearance revenue withheld in 2006 as well as that accrued in 2007;
- External budgetary financing in the second half of 2007 that would be around the same level as in the first half of the year of about \$0.5 billion (giving a total for 2007 of about \$1 billion);
- Minimal recourse to domestic bank borrowing, except for short-term bridge loans. Financing from the PIF would be used to repay government loans (in particular through the liquidation of some of its assets held as collateral by banks);
- Expenditure commitments that are in line with available cash resources (budgetary revenue, including clearance revenue from amounts withheld in 2006, and external financing) in the second half of 2007. All wage commitments for 2007 are envisaged to be met in full during the year, including to PA employees in Gaza. Nonwage spending commitments are envisaged to be sufficiently restrained to prevent arrears accumulation in the second half of 2007. However, for the year as a whole, reflecting the fact that expenditure tightening has started late in the year, about \$240 million in nonwage expenditure arrears are assumed to accumulate.

18. It is clear that the deficit yielded by the emergency budget, projected at 34 percent of GDP, is unsustainable and can only be financed through exceptional factors. These include an unusually high level of external financing, expenditure arrears accumulation, and the transfer of clearance revenue from amounts withheld in 2006.⁹ The high deficit (at about twice the level recorded for 2005) partly reflects, in addition to reduced

⁸ There are significant uncertainties regarding public administration in Gaza, including the extent of integration of its revenue and expenditure within the budget. Since July 2007 virtually no tax revenue has been remitted to the budget, and budgetary expenditure has been largely limited to the payment of PA employees' wages. The emergency budget envisages that domestic revenue from Gaza will continue not to be remitted to the budget through the second half of 2007, but that Gaza-related budgetary expenditures will continue along the trend observed in 2006.

⁹ The continued accumulation of arrears in 2007 leaves the total stock of arrears accumulated in 2006 and 2007 at \$1.1 billion, or 23 percent of GDP. There are also arrears accumulated from before 2006, the stock of which is not yet estimated.

revenue due to the turmoil, the fact that the emergency budget took effect late in the year. In particular, the initiation of adjustment measures, notably the retrenchment of government workers and other actions to reduce spending, would have a limited impact on the deficit for the year as a whole.



19. The budget framework is subject to several downside risks:

- External financing could be significantly lower than the envisaged \$1 billion if donors do not disburse in the second half of 2007 amounts about equal to those disbursed in the first half;
- Expenditure commitments could exceed the level envisaged. With regard to the wage bill, political pressures could result in the reemployment of at least some of the 20,000 security employees. For nonwage spending, commitments by line ministries and agencies could exceed the budget ceilings in the absence of effective commitment control and cash planning and management systems;
- The uncertainties regarding the situation in Gaza could result in unanticipated emergency or humanitarian spending.

IV. PREPARATIONS FOR THE 2008 BUDGET AND MEDIUM-TERM FRAMEWORK

20. **Discussions between the Ministry of Finance (MoF) and line ministries have begun on a comprehensive budget for 2008 in the context of a three-year fiscal framework for 2008–10.** That framework was outlined in the 2008 budget circular finalized in August 2007, and is in line with the broad objectives of the Palestinian National Policy Agenda for 2008–10 recently endorsed by the Cabinet. In the 2008 budget circular, the MoF requested each agency and line ministry to provide detailed inputs for such a framework, including: (i) a statement of its core objectives for the next three years; and (ii) the financial resources required for the fulfillment of those objectives, with a special focus on 2008. The underlying fiscal strategy aims at putting government finances on a sustainable path through a gradual reduction in the wage bill in real terms, a streamlining of social transfers, and an improvement in the collection of utility fees.

21. While the medium-term strategy is still being elaborated, it is expected to be underpinned by the following core elements, as conveyed in the 2008 budget circular:

- The economic outlook for the medium term remains highly uncertain, given its dependence on the extent of relaxation of border restrictions and freedom of movement. As a conservative working baseline, these restrictions are envisaged to be relaxed modestly over time. On that basis, real GDP is projected to grow at a yearly rate of 3–4 percent during 2008–10. The rate of inflation is projected to continue to be modest at about 3 percent per year;
- Budgetary revenue is projected to increase only modestly from the 2007 levels, reflecting the slow recovery of economic activity, as well as the uncertainties regarding the situation in Gaza. Clearance revenue is envisaged to be remitted in full and on a timely basis by the GoI. Domestic revenue is projected to grow broadly in line with nominal GDP growth;
- External financing is expected to decline steadily over the medium term, reflecting a strategy of increased reliance on domestic resources for budget financing;
- A tight expenditure policy would be implemented, aimed at containing expenditures in line with available resources (budgetary revenue and external financing). That policy will consist of gradually reducing the wage bill in real terms, streamlining social transfers, and improving the collection of utility fees. New domestic payment arrears will be avoided, as will recourse to domestic bank borrowing except for short-term bridge loans;
- The functioning of the PFM system, and in particular its transparency and accountability, will continue to be enhanced to ensure full compliance with international standards and practices. All budgetary income and expenditure will be channeled through the Single Treasury Account (STA);
- Arrears accumulation will be avoided through the following steps: (i) the issuance of ministerial orders to ensure that all wage deductions, including for the contributions to the pension funds, are fully disbursed without delay; (ii) the disbursement of all welfare payments; and (iii) strengthening the work of controllers at the level of line ministers, and putting in place an effective commitment control and cash planning and management systems, to ensure that no commitments are made by the ministries beyond what is expected to be covered by cash transfers from the MoF;
- Work will continue on the integration of the investment budget into the overall PA budget, in particular to ensure: (i) the channeling of all project-related disbursements through subaccounts to the STA; (ii) the consolidation of the information on future investment provided by the donors into a comprehensive “development projects” database that is routinely updated; and (iii) monitoring the implementation of all

investment projects, in close coordination with the Ministry of Planning, and the preparation of periodic reports on the status of projects financed from the PA's own resources.

22. **Fulfilling these broad medium-term objectives will require the elaboration of strong and politically difficult measures.** In particular, a sustained reduction in the real wage bill will require strict adherence to employment ceilings and restraint in increases in wage rates, while allowing for adequate staffing in the areas of health and education. Improving the collection of utility bills will require measures to discontinue the provision of services to delinquent households, while targeting subsidies to the poorer groups. Similarly, many of the social benefits should be phased out to make way for an efficient social safety net. In addition, a medium-term plan to clear the large stock of arrears will be needed, which will be an additional burden on future budgets. As these measures will take time to implement fully, even with strong adjustment measures and normal transfers of clearance revenue, substantial donor budgetary assistance will remain essential over the medium term.

23. **A phasing out of the restrictions on movement and access imposed by the GoI is essential to sustain the adjustment process.** A relaxation of such controls would revive private sector activity and accelerate the pace of implementation of public investment projects, which would markedly raise economic growth. Higher growth would in turn broaden the tax base, increase private sector jobs for retrenched government workers, and reduce the need for social benefits and subsidies. Without a strong economic recovery, the PA would remain reliant on large external support, and a fiscal strategy based on austerity measures would continue to be politically challenging.

24. **The IMF staff's work in the WBG will intensify as the donor community fully reengages with the PA,** with a focus on the macroeconomic, fiscal, and financial areas. In particular, the staff will help in budget preparation and the development of a fiscal strategy underpinned by a macroeconomic framework. The staff could also play a useful role in the context of a possible new budget support instrument, notably by regularly reporting to donors on the macroeconomic and fiscal situation, and on the implementation of public finance reforms. Technical assistance will also be stepped up, including in the areas of public expenditure management, banking supervision and regulation, and macroeconomic statistics.

V. PUBLIC FINANCIAL MANAGEMENT

25. **The PFM system became increasingly fragmented following the imposition of financial sanctions in early 2006,** and much of the progress that had been made up to 2005 with the help of the international community was lost. Donors disbursed funds to the PA through channels outside the control of the MoF, and banks were reluctant to transact with the government for fear of sanctions. These channels included the Office of the President, the European Commission's TIM, and the PIF. As a result, the STA was suspended, and, without a proper budget framework and adequate central control, transparency and accountability were substantially reduced.

26. **During March-June 2007, in his capacity as Minister of Finance in the previous unity government, Mr. Fayyad worked to regain control over public finances**, within the constraints of the then prevailing financial sanctions. In May 2007 he established a “Palestine Liberation Organization” (PLO) Account for channeling external budgetary assistance. That account was under his direct control in his capacity as head of the PLO’s Department of Economic Affairs. In May and early June several donor countries disbursed funds through that account, which were mostly used to pay part of PA employees’ wages. The EU has continued to provide assistance through the TIM, which allowed the payment of fixed allowances to civil servants.

27. **The lifting of financial sanctions in June 2007 opened the way for restoring the MoF’s full control over public finances**, which in turn enabled the preparation of the emergency budget for 2007. The STA was reestablished at the ministry to enable the consolidation of all budgetary revenue and expenditure. This was facilitated by the normalization of relations with commercial banks.

28. **In July 2007, an IMF technical assistance mission reviewed the status of the PFM system.** One finding of particular importance to donors was that cash controls that existed prior to 2006 have largely been restored. At the same time, the mission noted that there is still scope for further improvement, notably by phasing out the special accounts established by donors, which would allow more efficient cash management. To further strengthen transparency and accountability, it will also be important to produce regular and timely monthly fiscal reports with the same rigorous methodology used to prepare the 2006 fiscal data presented in this report. There is also a need to address longstanding challenges to the PFM system, in particular through steps to improve cash management and the strengthening of controls on expenditure commitments at the level of line ministries.

Table 1. West Bank and Gaza: Selected Economic Indicators, 2003–2006

(Quota: N/A)				
(Population: 3.94 million; 2006)				
(Per capita GDP: US\$1,114; 2006)				
(Poverty rate: 58 percent, 2007)				
(Main Exports: Manufactured goods, food and live animals, and chemicals; 2005)				
	2003	2004	2005	Est. 2006
Output and Prices				
(Annual percentage change)				
Real GDP (1997 market prices)	5.8	6.0	6.0	-8.0
CPI inflation rate (end of period)	3.8	3.9	2.3	3.3
CPI inflation rate (period average)	4.4	3.0	3.6	3.6
GDP deflator (in dollar terms)	8.6	6.1	3.6	6.6
Investment and Saving				
(In percent of GDP)				
Gross capital formation, of which:	26.8	25.1	24.1	19.3
Nongovernment	18.8	17.5	16.7	15.1
Gross national savings, of which:	10.0	3.8	1.8	8.7
Nongovernment	12.7	5.3	3.3	9.7
Saving-Investment balance	-16.8	-21.3	-22.4	-10.6
Public Finances				
(In percent of GDP)				
Revenue 1/	20.6	23.4	27.5	26.5
Expenditure and net lending	35.2	37.5	44.5	53.0
Of which: current	29.4	32.8	35.9	44.2
capital 2/	1.0	0.9	1.0	0.3
net lending	4.8	3.9	7.7	8.6
Balance before external budget support	-14.6	-14.1	-17.0	-26.5
External budget support	7.2	8.7	7.8	16.8
Balance after external budget support	-7.4	-5.4	-9.2	-9.7
Residual (including arrears)	1.4	-0.2	-4.5	-0.2
Total government debt	...	...	...	...
Monetary Sector 3/4/				
(Annual percentage change, unless otherwise indicated)				
Credit to the private sector	0.2	23.6	27.4	7.9
Private-sector deposits	8	5	2.5	6.2
Interest rates: US \$ lending (in percent)	7.6	7.1	7.4	8.0
US \$ deposits (in percent)	0.8	1.6	2.6	3.4
External Sector 5/				
(In percent of GDP)				
Exports of goods and nonfactor services	12.8	13.1	13.1	12.2
Import of goods and nonfactor services	78.5	80.4	80.3	79.2
Net factor income	13.3	11.2	12.0	12.2
Net transfers	35.6	34.7	32.8	44.2
Official transfers	14.3	15.4	14.2	20.8
Current account balance (excluding official transfers)	-31.1	-36.7	-36.5	-31.4
Current account balance (including official transfers)	-16.8	-21.3	-22.4	-10.6
Foreign direct investment	...	...	...	...
Total external debt	...	...	...	...
Gross official reserves	...	...	...	...
Memorandum items: 6/				
Nominal GDP (millions of U.S. dollar)	3,624	4,077	4,478	4,391
Nominal GNI (millions of U.S. dollar)	4,105	4,534	5,017	4,926
Unemployment rate (average in percent of labor force)	25.6	26.8	23.5	23.6
Net imports of petroleum products	...	...	...	...
Exchange rate of New Israeli Shekel per U.S. \$ (period average)	4.55	4.48	4.49	4.46
Real effective exchange rate	...	...	...	...
Al Quds stock market index (annual percentage change)	19.0	54.4	306.6	-46.4

Sources: The Palestinian authorities, the World Bank, and Fund staff estimates.

1/ Includes clearance revenue transferred by Israel..

2/ Excludes foreign financed capital spending.

3/ End of period.

4/ Data on base and broad money, as well as the velocity of circulation are not available.

5/ Data on merchandise exports and imports, FDI, total external debt, and gross reserves are not available.

6/ Data on petroleum imports and on the real effective exchange rate are not available.

Table 2. West Bank and Gaza: Central Government Fiscal Operations (cash basis), 2004–07

	2004 1/	2005 1/	2006	2007 Budget
	(In millions of U.S. dollars)			
Revenue	1,051	1,370	739	1,327
Gross domestic	337	476	395	294
Tax revenues	191	231	238	178
Non-tax revenues	146	245	157	117
Gross clearance revenue	713	894	344	1,033
Expenditure and net lending	1,528	1,994	1,443	2,327
Gross wages and allowances	870	1,001	658	1,368
Non-wage current expenditure 2/	465	605	398	444
PA financed capital spending	36	44	12	15
Net lending	157	344	376	500
Balance	-477	-625	-704	-1,000
External budget support 3/	353	349	738	1,000
Balance after budget support	-124	-276	34	0
Total other financing	124	276	-34	0
PIF profits and advances	0	173	146	70
Net domestic bank financing	134	304	-171	-70
Residual	-9	-202	-8	0

Sources: Ministry of Finance, Office of the President, Palestinian Investment Fund, European Commission, World Bank; and IMF staff estimates.

1/ For 2004 and 2005, comprehensive data on arrears accumulation are not available.

2/ Includes expenditure for domestic tax refunds

3/ External financing in 2006 includes only documented amounts.

Table 3. West Bank and Gaza: Central Government Fiscal Operations (commitment basis), 2004–07

	2004 1/	2005 1/	2006	2007 Budget
	(In millions of U.S. dollars)			
Revenue	954	1,232	1,165	991
Gross domestic	337	476	395	294
Tax revenues	191	231	238	178
Non-tax revenues	146	245	157	117
Gross clearance revenue	617	757	770	697
Expenditure and net lending	1,528	1,994	2,327	2,566
Gross wages and allowances	870	1,001	1,189	1,368
Non-wage current expenditure 2/	465	605	750	683
PA financed capital spending	36	44	12	15
Net lending	157	344	376	500
Balance	-574	-762	-1,162	-1,575
External budget support 3/	353	349	738	1,000
Balance after budget support	-221	-413	-424	-575
Total other financing	221	413	424	575
Net expenditure arrears accumulation (+)	...	...	884	239
Net clearance revenue arrears accumulation (-)	97	137	-427	336
PIF profits and advances	...	173	146	70
Net domestic bank financing	134	304	-171	-70
Residual	-9	-202	-8	0

Sources: Ministry of Finance, Office of the President, Palestinian Investment Fund, European Commission, World Bank; and IMF staff estimates.

1/ For 2004 and 2005, comprehensive data on arrears accumulation are not available.

2/ Includes expenditure for domestic tax refunds

3/ External financing in 2006 includes only documented amounts.

Table 4: West Bank and Gaza: Central Government Fiscal Operations, 2004–07

	2004	2005	2006	2007 Budget
(In millions of U.S. dollars)				
Revenue	954	1,232	1,165	991
Gross domestic	337	476	395	294
Clearance (accrued)	617	757	770	697
Clearance (cash)	713	894	344	1,033
Clearance (net arrears accumulation)	-97	-137	427	-336
Gross arrears accumulation	0	0	770	0
Gross arrears repayment	97	137	344	336
Total expenditure and net lending (on a commitment basis) 1/	1,528	1,994	2,327	2,566
Wage expenditure (commitment)	870	1,001	1,189	1,368
Wage expenditure (cash)	870	1,001	658	1,368
Wage expenditure (net arrears accumulation)	...	...	532	0
Non-wage current expenditure (commitment)	465	605	750	683
Non-wage expenditure (cash)	465	605	398	444
Non-wage expenditure (net arrears accumulation)	...	...	353	239
PA-financed capital expenditure	36	44	12	15
Net lending	157	344	376	500
Balance (commitment basis)	-574	-762	-1,162	-1,575
add: expenditure arrears (net accumulation)	...	...	884	239
subtract: net clearance withheld (+) or transferred from past collections (-)	-97	-137	427	-336
Balance (cash basis)	-477	-625	-704	-1,000
add: external budgetary support	353	349	738	1,000
Balance (commitment basis, after external support)	-221	-413	-424	-575
Balance (cash basis, after external support)	-124	-276	34	0
Total other financing (other than external support)	124	276	-34	0
Advances and other payments by Palestinian Investment Fund	0	173	146	70
Net domestic bank financing	134	304	-171	-70
Residual	-9	-202	-8	0
Memorandum items:				
Revenue, as a share of GDP	23	28	27	22
Expenditure and net lending, as a share of GDP	37	45	53	56
Balance before external support, as a share of GDP	-14	-17	-26	-34
GDP	4,077	4,478	4,391	4,596
Stock of withheld clearance revenue 2/	-	-	427	-

Sources: Ministry of Finance and IMF staff estimates.

1/ For 2004 and 2005, comprehensive data on arrears accumulation are not available.

2/ The stock of withheld clearance revenue in 2006 is net of deductions of amounts owed by the PA to Israeli private enterprises, and includes the amounts attached by the courts (estimated at about \$85 million as of July 15, 2007, using an exchange rate of 4.47 \$ per NIS).

Table 5. West Bank and Gaza: External Budget Support 2005-06 1/

	2005	2006
	(In millions of U.S. dollars)	
PA government 2/ 3/	349	236
Bilateral donors	194	193
Arab countries	194	182
Other countries	0	12
Multilateral donors 4/	155	43
Office of the President	...	275
Arab countries	...	264
Other	...	10
EC Interim Emergency Relief Contribution	...	56
Temporary International Mechanism 4/	...	172
Total	349	738

Sources: Ministry of Finance, Office of the President, European Commission, World Bank; and IMF staff estimates.

1/ External budget support provided for recurrent spending.

2/ External financing in this table includes only documented amounts.

3/ Assistance to the PA government was channeled through accounts under the control of the ministry of finance.

4/ Includes part of the World Bank's Emergency Services Support Program.