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Main reports

The Palestine Monetary Authority Business Cycle Index (PMABCI) improved to -12.1 points in March 2017 from -12.3 points last month

During 2016, the total volume of olive oil extracted in Palestine decreased by 4.5% when compared to 2015, corresponding to a 11.6% drop in the total volume of olives pressed during the same period

Palestinian and Israeli officials signed an agreement on 5 April 2017, enabling Palestinian mobile service providers to offer 3G services

The Al-Quds index increased by 1.61% during March 2017, reaching 538.9 points on the last day of trading

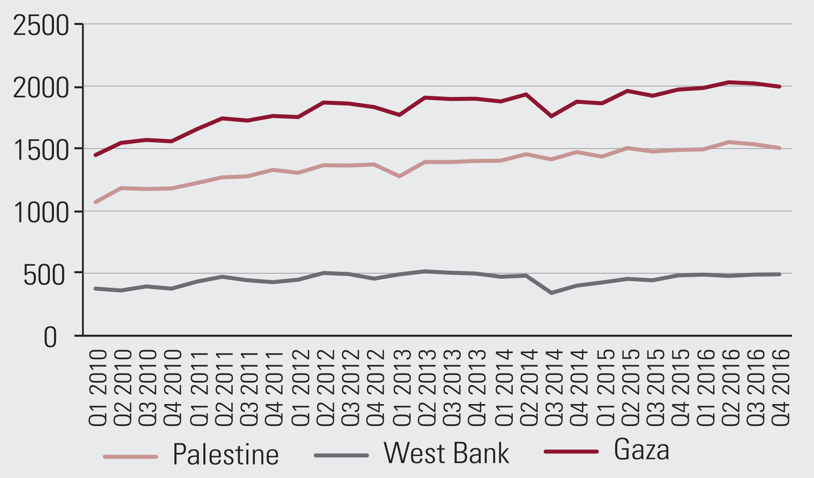
This month the Bulletin interviews Dr. Luis Abugattas, a Palestinian-Peruvian expert on trade policies and development

National Accounts

According to preliminary estimates by the Palestinian Central Bureau of Statistics (PCBS), real GDP in Palestine reached $1,997.3m in Q4 2016, which is a 1.3% decrease compared to the previous quarter but a 1.3% increase when compared to Q4 2015.[1] Year-on-year country-level real GDP increased by 4.1% in 2016 compared to 2015.[2]

Real GDP in the West Bank reached $1,505.3m in Q4 2016, a decrease of 1.9% from Q3 2016, mainly due to an 8.6% drop in wholesale and trade activities. In Gaza, real GDP was $492m, marking a 0.5% increase from Q3 2016, with Gazan GDP overall remaining close to flat since Q1 2010.

Figure 1: Quarterly Real GDP by Region (Base-Year: 2004), Q1/2015-Q4/2016 (million $)



Source: PCBS

Real GDP per capita in Palestine reached $434.2 in Q4 2016, down 1.5% from Q3 2016 and 2.0% from Q4 2015. In the West Bank, real GDP per capita reached $558.5, a decrease of 1.3% from Q3 2016 and 2.5% from Q4 2015. In Gaza, real GDP per capita reached $258.3, down 2.2% from Q3 2016 and 2.1% from Q4 2015.

Business Cycle Index

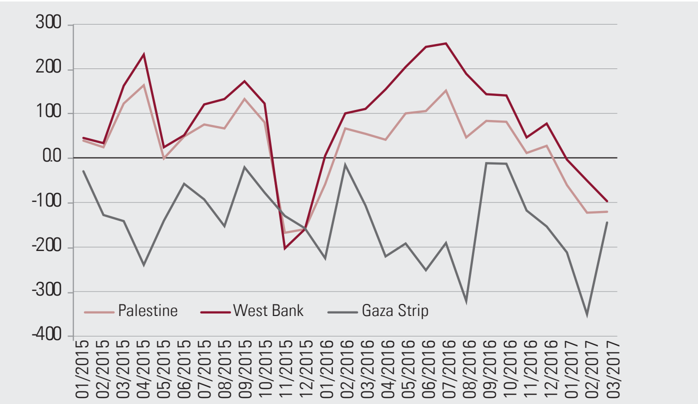
In March 2017, the Palestine Monetary Authority Business Cycle Index (PMABCI) improved to -12.1 points from -12.3 points last month but year on year remains down from 4.0 points in March 2016.[3]

In the West Bank, the index dropped to -9.7 points in March 2017 from -5.1 points in February 2017. The fall was attributed to decreases across sectoral indices, most significantly in the food and construction indices. Furthermore, business owners indicated inventories accumulation throughout March, which implies lower expectations regarding production in coming months.

1 www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_28-3-2017-NA-en.pdf
2 A more detailed report on the 2016 annual GDP figures will be added once the complete data has been released by the PCBS (expected in December 2017).
3 www.pma.ps/Default.aspx?tabid=205&ArtMID=793&ArticleID=1074&language=en-US

In Gaza, the index improved to -14.5 points in March 2017 from a low of -35.1 points in February 2017. The improvement was driven by positive changes in the indices of all sub-sectoral activities, except for a decline in the plastics industry. The Gaza index has been negative since August 2013 (except for October 2013) because of its particularly poor economic situation. The electricity crisis in Gaza is often cited as the main reason for the persistent decline of the Gaza index.

Figure 2: Monthly PMABCI, January 2015 - March 2017 (Points)



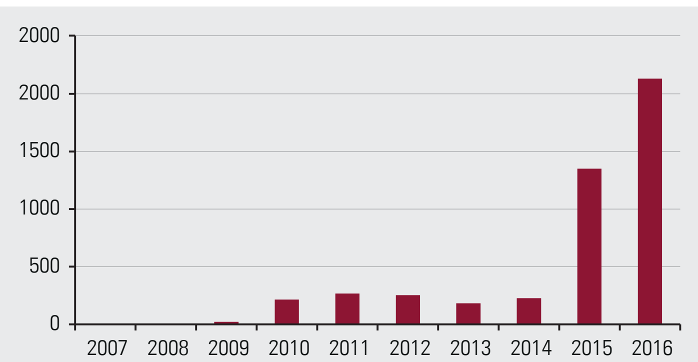
Source: PMA

The PMABCI is a monthly index measuring the state of industrial activities and trends in Palestine based on surveys distributed to owners of around 200 private sector companies from different industrial sub-sectors across the West Bank and Gaza.

Snapshot: Olive Pressing Activities

According to recently published data, a total of 84,100 tonnes of olives were pressed in 2016, extracting a total of 20,100 tonnes of olive oil.[4] Compared to 2015, these figures mark a decrease of 11.6% in the volume of pressed olives and 4.5% in the volume of extracted olive oil. However, the extraction rate[5] improved in 2016 to reach 23.9%, compared to 22.2% in 2015.

Figure 3: Pressed Olives and Extracted Olive Oil, 2003-2016 (Tonnes)



Source: PCBS

Olive and olive oil production are concentrated in the West Bank, which holds 245 of the 274 olive presses in Palestine. Most Palestinian olives (76.2%) are pressed in the West Bank, producing 81.6% of total olive oil volumes in Palestine.

The olive sector is a major part of agricultural activities in Palestine. Nearly half of total agricultural land in the West Bank and Gaza is cultivated with olive trees. The United Nations Office for the Coordination of Humanitarian Affairs (OCHA) estimates that between 80,000 and 100,000 families rely on olives and olive oil for primary or secondary sources of income. The sector employs large numbers of unskilled laborers and approximately 15% of all working women. The entire olive sector, including olive oil, table olives, pickles and soap, is worth between $160m and $191m in high-yield years.[6]

Balance of Payments

In Q4 2016, the Palestinian current account deficit increased by 16.1% from the previous quarter, reaching $365.1m.[7] The increase was caused by a growing deficit in the trade balance of goods and services of 5.6% and 4.9%, respectively. In Q4 2016, total exports amounted to $253.6m and total imports to $1,334.0m.

The income account, which includes compensation of employees and investment income, recorded a surplus of $408.6m, up by 1.8% from Q3 2016. Compensation of Palestinian employees working in Israel formed most of the surplus ($396.7m).

The capital and financial account recorded a surplus of $354.5m, up 25.9% from Q3 2016. The surplus in the financial account increased 7.6% to reach $209.8m, and the surplus in the capital account reached $144.7m, up from $86.6m in Q3 2016. Reserve assets at the Palestine Monetary Authority (PMA) decreased from $89.2m in Q3 2016 to $22.6m in Q4 2016.

Table 1: Balance of Payments Q4 2015, Q3 2016 and Q4 2016

Item	Q4 2015 (USD millions)	Q3 2016 (USD millions)	Q4 2016 (USD millions)	Change (%) (Q4 2015-Q4 2016)	Change (%) (Q3 2016-Q4 2016)
Current Account	**-449.8**	**-314.4**	**-365.1**	**-18.83%**	**16.13%**
Trade Balance of Goods	-1268.9	-1066.8	-1126.6	-11.21%	5.61%
Trade Balance of Services	-45.8	-221.7	-232.5	407.64%	4.87%
Income Balance	347.5	401.3	408.6	17.58%	1.82%
Balance of Current transfers	517.4	572.8	585.4	13.14%	2.20%
Capital and Financial Account	**570.4**	**281.6**	**354.5**	**-37.85%**	**25.89%**
Net Capital Account	112.3	86.6	144.7	28.85%	67.09%
Net Financial Account	458.1	195.0	209.8	-54.20%	7.59%

Source: PCBS and PMA

4 www.pcbs.gov.ps/Downloads/book2258.pdf
5 The total weight of olive oil produced as a percentage of the total weight of olives pressed

6 http://bit.ly/2q9BPld
7 www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_28-3-2017-BP-en.pdf

International Investment Position and External Debt

The stock of investments of Palestinian residents outside Palestine (total external assets) exceeded investments in Palestine by non-residents (total foreign liabilities) by $1,289m in Q4 2016.[8] Palestine's International Investment Position (IIP, defined as external assets minus foreign liabilities) increased by $14m (1.1%) from the previous quarter. The rise was the result of a $173m decrease in foreign liabilities partially offset by a $159m decrease in external assets.

Table 2: International Investment Position (IIP) Stock, Palestine, Q4 2015, Q3 2016 and Q4 2016

Item	Q4 2015 (USD millions)	Q3 2016 (USD millions)	Q4 2016 (USD millions)	Change (%) (Q4 2015-Q4 2016)	Change (%) (Q3 2016-Q4 2016)
International Investment Position (Net)	**899**	**1,275**	**1,289**	**43.38%**	**1.10%**
Total External Assets	**5,855**	**6,297**	**6,138**	**4.83%**	**-2.53%**
Foreign Direct Investment Abroad	352	444	445	26.42%	0.23%
Portfolio Investments Abroad	1,084	1,159	1,110	2.40%	-4.23%
Other Investments Abroad	3,838	4,359	4,270	11.26%	-2.04%
Of which: Currency and Deposits	3,815	4,010	3,921	2.78%	-2.22%
Reserve Assets	581	335	313	-46.13%	-6.57%
Total Foreign Liabilities	**4,956**	**5,022**	**4,849**	**-2.16%**	**-3.44%**
Foreign Direct Investment in Palestine	2,486	2,570	2,588	4.10%	0.70%
Foreign Portfolio Investments in Palestine	821	750	658	-19.85%	-12.27%
Foreign Other Investments in Palestine	1,649	1,702	1,603	-2.79%	-5.82%
Of which: Loans from Abroad	1,119	1,118	1,104	-1.34%	-1.25%
Of which: Currency and Deposits	530	581	496	-6.42%	-14.63%

Source: PCBS and PMA

The gross external debt amounted to $1.6bn at the end of Q4 2016, a decrease of 5.8% from the previous quarter and 2.6% compared to Q4 2015. The debt of the general government (central, state and local government) constituted 65.0% of total debt, while private bank debt amounted to 30.9%. The debt of other sectors (non-financial, insurances, NGOs and households) constituted 4.1% of the total.

3G in Palestine

On 5 April, the Undersecretary of the Palestinian Ministry of Telecommunications and Information Technology, Mr. Suleiman Al-Zuheiri, and a representative of the Israeli Ministry of Communication signed an agreement enabling Palestinian mobile service providers to offer 3G services.[9] The rollout of 3G is expected to be an important step in the development of the Palestinian telecommunications sector and the Palestinian economy. The agreement follows a memorandum of understanding that was signed in November 2015 but was subsequently followed by extensive negotiations on implementation. Per the 2015 agreement, Jawal and Wataniya, the West Bank's two mobile network operators, will be allocated 20 megahertz (Mhz) of 3G frequencies.[10] Wataniya, a member of the Qatari Ooredoo Group, also announced that it is due to launch services in Gaza after a delay period that lasted eight years.[11]

When 3G licenses were first auctioned by the Government of Israel, Palestinian providers were excluded citing Israeli security concerns. Palestinian operators have since operated at a competitive disadvantage with over 20% of the Palestinian market captured by unauthorised Israeli operators according to a 2016 World Bank report[12]. The report states that the Palestinian mobile sector had lost over $1bn in potential revenue as well as that the Palestinian National Authority (PNA) has experienced $184m in fiscal losses between 2013 and 2015, primarily due to the absence of 3G capabilities.

March Trading

The Al-Quds index increased by 1.61% during March 2017, reaching 538.9 points on the last day of trading.[13] The index experienced a positive trend throughout March, peaking at 541.8 points on 29 March. A total of 16.1m shares worth $28.4m were traded, marking a 47.2% and a 23.8% increase in the number and value of traded shares, respectively. The insurance services sector witnessed the highest increase (3.2%), while banking and financial services faced the largest drop (-0.51%).

Interview with Dr. Luis Abugattas

This month the Bulletin interviews Dr. Luis Abugattas, a Palestinian-Peruvian expert on trade policies and development. Dr. Abugattas leads the project "EU Support to the Ministry of National Economy for Trade Policy Formulation and WHO Accession". Dr. Abugattas has been involved in Palestinian trade policy issues for over 20 years and has served as advisor to several Palestinian ministers on trade issues and private sector development.

What are the major challenges facing the Palestinian export sector? What are the opportunities?

The main challenge is moving through a path of growth-enhancing structural change, towards a high-technology, high-productivity economy. Fifty years of occupation generated significant distortions in the structure of the Palestinian economy including a hypertrophic services sector. Palestine has perhaps the highest contribution of services to GDP worldwide based on income per capita levels, while the tradable sector is significantly underdeveloped. I'd like to use Galbraith's concept of "symbolic modernization" to describe the situation in Palestine – some iconic public buildings, some

8 www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_19-3-2017-IP-en.pdf
9 www.maannews.com/Content.aspx?id=776293

10 http://bit.ly/2p4gTxt
11 http://english.wafa.ps/page.aspx?id=Lv1XtHa74427084600aLv1XtH
12 http://bit.ly/2bR2rmR
13 www.pex.ps/PSEWebSite/publications/1004201702.pdf

infrastructure development and some highly visible private investments, but the economic fundamentals have not improved. The trade challenges are on the supply side. Exports include olive oil, stone and marble and furniture and constitute 7% of GDP, when the average for lower middle-income countries is 17%.

The main developmental problems are trade policy having been conditioned by the Paris Protocol and national developmental plans never prioritising trade policy. The latter is changing as the new national strategy gives more attention to trade policy. With regards to industrial policies, all efforts have been focused on improving the business environment, with little if any support at the firm level. The private sector remains significantly underdeveloped, with only 81 manufacturing companies employing more than 50 workers. Most of the economy is comprised of family-run micro and small enterprises with a high proportion of family workers.

Who are Palestine's key strategic trade partners and what is the way forward to enhance trade with them?

Palestine is exporting around $10m to Europe per year, $5m to the US and practically nothing to Canada although we have free market access. The most utilised agreement is the Greater Arab Free Trade Agreement (GAFTA). The problem is that there is no supply-side capacity. Palestine does not have the products which the world market is demanding. You cannot export what you produce; you should export what the world wants. Even in GAFTA, 67% of the increase in exports is due to olive oil, stone and marble. The way forward is to look at what the world wants and what of that Palestine can produce and then implement industrial policies to develop those sectors.

What is the optimal trade regime under the current circumstances?

Soon our project will present a proposal of trade policy for Palestine, including a tariff component. In a study that will be published by MAS soon, we are analysing what would be the most appropriate tariff policy. What is clear is that the Paris Protocol arrangements are completely dysfunctional for the Palestinian economy. The tariff schedule adequate for Israel is not adequate for Palestine, which needs to use tariffs as an instrument of industrial policy – to lower the cost of some inputs and protect sectors that have potential. It is the typical "infant industry" argument. New companies need time to become competitive.

What is the significance of potential accession to the WTO? What are the next steps towards its realisation?

Palestine is de facto implementing all WTO obligations, because of the Paris Protocol and because Israel is a member, without receiving any benefits. The main benefit is the availability of the dispute settlement mechanism, a forum where small countries can defend their interests. Another one is that the WTO agreements are international best practices in many areas, such as technical standards and trade facilitation for the private sector, so being a member would allow Palestine to put its house in order.

It will take time. You must be an observer for five years before starting accession negotiations, which last up to ten years. Palestine requested an observer status in 2009, but no action was taken. Now the Government is exploring the possibility of presenting another request. The project has supported the MoNE in that endeavor, and it is now a political decision.

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The Palestinian Economic Bulletin is prepared by the Palestine Economic Policy Research Institute (MAS) and edited by The Portland Trust. Please send any comments, suggestions, or complaints to feedback@portlandtrust.org

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