MACROECONOMIC AND FISCAL FRAMEWORK
FOR THE WEST BANK AND GAZA:
FOURTH REVIEW OF PROGRESS[1]

STAFF REPORT FOR THE MEETING OF THE AD HOC LIAISON COMMITTEE

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[1] This report was prepared by a team composed of Oussama Kanaan (Chief of Mission), Rina Bhattacharya, and Roman Zytek. The macroeconomic and fiscal framework set out in the Palestinian Reform and Development Plan (PRDP) was assessed by IMF staff in "Medium-Term Macroeconomic and Fiscal Framework for the West Bank and Gaza," issued on December 5, 2007 (SM/07/384). The report on the third review of progress in implementing the framework was issued on February 25, 2009 (FO/Dis/09/24). Staff reports on the West Bank and Gaza are published on the IMF website (www.imf.org/wbg).

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EXECUTIVE SUMMARY

There is a realistic chance that the downward trend in Palestinians' living standards can be reversed in the near future, at least in the West Bank, provided that restrictions on movement and access continue to be eased. Security reforms by the Palestinian Authority (PA), including the reestablishment of law and order in major West Bank cities, were complemented by the relaxation of restrictions on movement and access in expanding private sector activity. However, Gaza's situation remains difficult, despite some easing of Gaza's blockade. Provided remaining restrictions in the West Bank are lifted in the remainder of the year, real GDP in the West Bank is projected to rise by about 7 percent in 2009, which would represent the first substantial increase in living standards since 2005. However, assuming only a limited easing of its blockade, Gaza's real GDP per capita would decline further, although at a slower pace than in 2008.

The PA has continued with institution-building and prudent fiscal policies. These policies, along with progress in public expenditure management and good governance, have bolstered private sector confidence. Discipline in containing growth in public sector wage rates and employment has continued, and utility subsidies are being phased out. However, the war in Gaza has imposed a substantial burden on the budget. While total donor aid during January to August 2009 was generous, in line with the original 2009 budget, over half of it was disbursed as late as in July and August. The Gaza war and delays in donor aid has worsened an already difficult liquidity situation and led to substantial government borrowing from commercial banks as well as arrears accumulation in the first half of the year. It is particularly important for the PA to keep budgetary expenditures in line with the 2009 budget target, notably by restraining non-wage spending.

There is a need to secure adequate and timely donor assistance to finance the budget deficit in the remainder of 2009 and 2010. External recurrent financing requirements for September to December 2009 are projected at about $0.4 billion, including emergency spending for Gaza. This amount is in addition to a minimum of $1.1 billion required for public investment and reconstruction in the Palestinian territories for 2009–10. Continuation of fiscal retrenchment, combined with lower projected emergency spending for Gaza, will result in a substantial reduction in the recurrent budget deficit from $1.5 billion in 2009 to $1.2 billion in 2010.

Close cooperation between the three parties, the PA, the government of Israel, and donors, is critical to ensure the success of reforms and a sustained rise in living standards. Perseverance by the PA in the implementation of the Palestinian Reform and Development Plan, supported by adequate and timely donor assistance, is essential to support higher growth and a steady move toward fiscal sustainability. Risks to the economic outlook would be substantially reduced by a breakthrough in the peace process and the lifting of restrictions on trade not only within the Palestinian territories, but also between the territories and Israel. Indeed, especially given the absence of a functioning seaport and airport, the elimination of these restrictions is essential for an expansion in the West Bank and Gaza's external trade, which in turn is key to a sustained rise in real GDP per capita beyond 2009.

I. RECENT ECONOMIC DEVELOPMENTS

1. **While the macroeconomic situation in the West Bank has improved, conditions in Gaza remain difficult due to the blockade.** While the Gaza blockade has been relaxed somewhat compared to the situation leading up to the war in late 2008/early 2009, restrictions on non-humanitarian goods remain tight. In the West Bank two key factors have bolstered confidence and growth so far in 2009. First, there has been a substantial improvement in security conditions reflecting the redeployment of Palestinian Authority (PA) forces in major West Bank cities. The latter's impact on confidence has been complemented by the PA's public finance reforms, including a prudent expenditure policy that enabled the repayment of wage arrears. Second, restrictions on internal trade and the passage of people have been relaxed significantly.[2] Real GDP growth in the West Bank and Gaza (WBG) is estimated at about 6 percent in the first quarter of 2009 compared to the first quarter of 2008.

2. **The impact of the global recession on the Palestinian economy has thus far been limited.** While the global recession is lowering growth in Israel, its impact on the WBG is limited by the small share of its exports in GDP due to the long-standing restrictions on the Palestinian areas' exports to Israel. Two other potential areas of vulnerability include the West Bank and Gaza (WBG)'s reliance on donor aid and remittances from Diaspora Palestinians. However, so far donor disbursement decisions have been generally dominated by domestic and political factors (rather than the global recession), and there are no indications so far of a significant decline in remittances. On the positive side, the recession has had an indirect beneficial impact on Palestinian production costs and real household incomes as world food and fuel prices have been falling so far in 2009.

3. **While the unemployment rate has declined somewhat, it remains high, especially in Gaza**. The unemployment rate for the first half of 2009 is estimated at about 18 percent in the West Bank and 37 percent in Gaza, only slightly lower than in the first half of 2008. The unemployment rate in the West Bank is expected to continue to decline in line with the pick up in growth, albeit with a lag, provided that the easing of restrictions on movement and access is perceived as durable by the private sector. Gaza's prospects are more uncertain in the absence of indications that the blockade will be lifted in the near future. According to the August 2009 OCHA report, several of Gaza's welfare indicators have worsened in 2009.[3] Also, while restrictions on the entry of cash have eased somewhat compared to the situation in late 2008, their complete lifting is important to prevent the recurrence of cash shortages.

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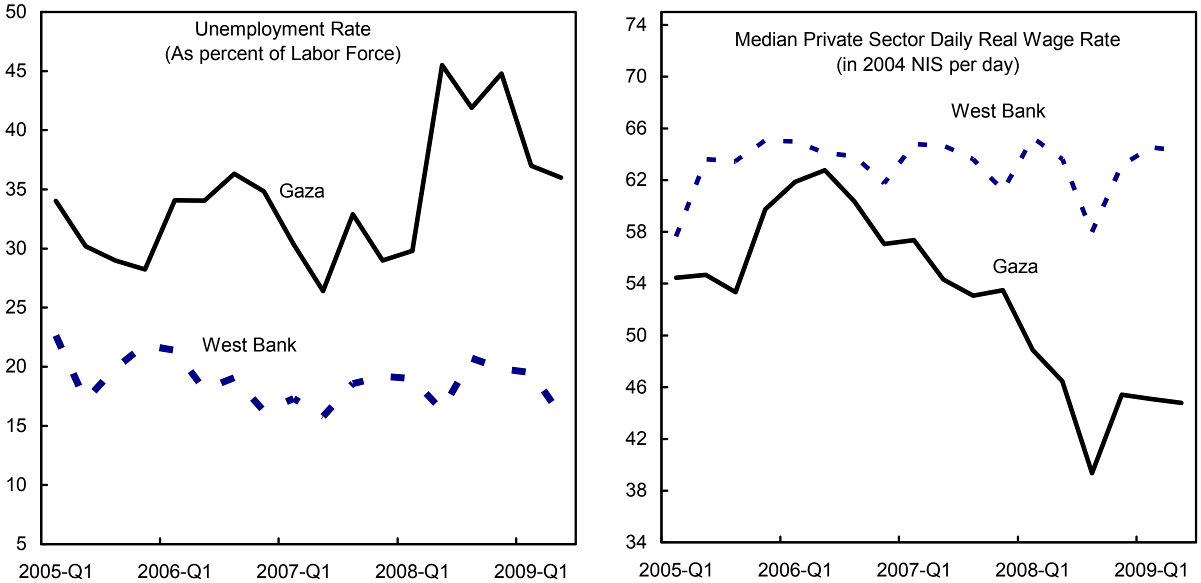
[2] As detailed in the UN Office for the Coordination of Humanitarian Affairs (OCHA), during 2009 the Israeli authorities have implemented several measures that have eased restrictions on movement and access affecting the West Bank cities of Nablus, Qalqiliya, Ramallah and Jericho. These measures have significantly reduced the amount of time required for people and goods to enter and leave these cities. For updates, see www.ochaopt.org.

[3] See OCHA's "The Humanitarian Impact of Two years of Blockade on the Gaza Strip," August 2009, www.ochaopt.org.

Figure 1. Divergent Labor Market Conditions in West Bank and Gaza

In the West Bank, the rate of unemployment and the median private sector real wage have remained broadly stable during the period 2007 to 2009, in contrast to the deterioration in Gaza.



Sources: Palestinian Central Bureau of Statistics; and IMF staff estimates.

4. **Inflation has declined sharply from its peak in mid-2008.** The twelve-month CPI inflation rate fell from 12 percent in July 2008 to about 2 percent by mid-2009, mostly reflecting the decline in world food and petroleum prices. The impact of the decline in world food prices on inflation has been more pronounced than in Israel, due to food's higher weight in the West Bank and Gaza's consumption basket. The inflation rate is still higher in Gaza (3 percent in mid-2009) than in the West Bank (-1 percent), reflecting the impact of the blockade. Given the importance of dollar-denominated sources of income such as part of remittances and donor assistance, the favorable impact of inflation on real incomes has been compounded by the depreciation of the shekel vis-à-vis the dollar by about 17 percent in the year to June 2009.

5. **The growth of deposits and private credit remains steady in the West Bank, but has been constrained in Gaza.** Deposits rose by 21 percent in real terms in the WBG in the year to June 2009, in line with improved economic conditions. Private sector credit in the West Bank, after falling steadily since 2006, rose by about 30 percent in real terms in the year to June 2009, due to both a better investment climate in major West Bank cities, as well as a rise in the required domestic lending-to-deposit ratio, set by the Palestine Monetary Authority (PMA), from 35 percent to 45 percent. However, in Gaza private sector credit fell by 11 percent in real terms over the same period, reflecting subdued activity and limited investment demand.

6. **The banking sector has been largely insulated from the global financial crisis.** The banking sector is overall well capitalized, with limited exposure to global financial markets, reflecting tight prudential regulations and conservative bank lending practices.[4] About 95 percent of banks' assets are placed in overseas government-guaranteed bank deposits. The remainder is invested in securities, shares and foreign loans, with a broad diversification across financial institutions and countries. The PMA has continued with institutional reforms to further strengthen the banking sector (Box 1).

7. **Risks to the balance sheets of some banks persist, due in particular to Gaza's continued isolation and its precarious security situation.** These risks have increased since late 2008 following tight restrictions on the entry of cash into Gaza and the severance by Israeli banks of correspondent relations with Gaza banks. The Palestinian and Israeli authorities have been working to ensure predictable passage of adequate amounts of cash from West Bank banks to their branches in Gaza. Another problem both parties are trying to resolve is the refusal of Israeli banks, on concerns about possible legal constraints, to accept cash deposits from West Bank banks, which is lowering the latter banks' interest income and raising insurance costs.

Box 1. Reforms by the Palestine Monetary Authority

The Palestine Monetary Authority (PMA) has continued institutional reforms, supported by IMF technical assistance. It has made considerable progress in 2007–08 in developing its Strategic Transformation Plan with the medium-term objective of becoming a full-fledged central bank. Additional steps were taken in 2009 in several areas:

- **The supervision and regulatory framework** was further strengthened. The PMA has developed a roadmap for the implementation of Basel II standards which will enhance the supervision of foreign banks operating in the WBG. New regulations for the licensing and supervision of money changers, including with regard to minimum capital requirements, have been issued in December 2008, and have been applied as of February 2009. In February 2009, a corporate governance code was implemented to ensure that banks adopt corporate governance lending practices in line with international standards. "Fair Lending" regulations have been implemented since March 2009 to standardize and improve the quality of information on banks' credit policies and conditions available to potential borrowers and guarantors. Regulations for the licensing and supervision of microfinance institutions were drafted and sent to the Cabinet in June 2009.
- The operation of **the credit registry** was further enhanced to allow banks to better evaluate risks, reduce collateral requirements, and improve credit flow. In April 2009, the microfinance institutions signed a memorandum of understanding with the PMA to enable the integration of their borrowers in the registry. In April 2009 the process of selecting a company to develop a credit scoring system started, with the aim of meeting Basel II standards by 2010.
- Progress was made in developing **an electronic payment system**, which will raise bank payments' efficiency and help reduce liquidity risk. This will include the Real Gross Time Settlement System and the Automated Clearance House. An agreement was signed in December 2008 with a private company to help set up the system.
- To further strengthen **the financial sector legal framework**, drafts of a new Banking Law and a Central Bank Law were submitted to the Cabinet in early 2009, and are expected to be approved by end-2009.

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[4] The value of non-performing loans (NPLs) and watch list loans has been falling as a share of total bank loans, and are more than fully covered by NPL provisions. Tier 1 capital is estimated to have reached 32 percent of risk-weighted assets in June 2009, up from 27 percent at end-2007.

II. Fiscal Developments

8. **In the first half of 2009, fiscal developments were significantly influenced by the war in Gaza:**

- Budgetary "net revenue," excluding one-off items such as dividend payments and license fees,[5] were broadly in line with the budget, with lower-than-expected clearance revenues offset in part by better collection of fees and charges and lower tax refund payments. Tax refund payments are expected to rise in the remainder of 2009 to meet the full budgeted amount, thus reducing net revenues compared to the first half of the year. The contraction of Gaza's economic activity and imports due to the war and tightened blockade led to a sharp fall in its clearance revenues.

- The wage bill for the first half of the year was broadly in line with the pro-rated budget. As envisaged in the budget, there was a general wage rate increase in early 2009 by 4 percent, and a rise in net public sector employment by less than 3,000 employees.

- As the 2009 budget was passed before the onset of the war in December 2008, it did not envisage any war-related emergency spending. On August 24th an amendment to the budget was issued by the Council of Ministers, which adds $300 million in emergency spending to address the fiscal consequences of the war in Gaza.

- The $300 million envisaged in the budget amendment reflects the PA's intention to assume increasing responsibility for Gaza's emergency recovery projects, the bulk of which has hitherto been directly funded and implemented by UN agencies and NGOs.[6] Out of the $300 million, about $78 million has already been spent during January to June 2009 largely on cash assistance to families affected by the loss of sources of income and shelter due to the war. The remainder $220 million is intended broadly for emergency projects to rehabilitate the water, sanitation and electricity networks. The authorities stated that the latter amount would only be spent under two conditions. First, aid should become available for this purpose, in which case the details of such spending

[5] The 2009 budget envisaged receipt of about $140 million in telecommunication license fees. While no such fees were received in the first half of 2009, about $200 million in fees is expected before end-2009 as a result of the Zain-Paltel telecommunications merger.

[6] Emergency aid for Gaza's recovery after the war has been mostly disbursed by donors directly through UN agencies and NGOs. Discussions have been underway in 2009 between the PA and UN agencies to establish a Trust Fund to coordinate the funding and implementation of the UN projects in Gaza. The Trust Fund is expected to be established and become operational when Gaza's blockade is eased to allow the passage of capital goods and raw materials. For details on emergency projects in Gaza, see the UN reports published on www.ochaopt.org/gazacrisis .

would be decided in close coordination with donors. Second, an easing of Gaza's blockade would be needed to allow the passage of raw materials and capital goods necessary for the projects' implementation.

- Non-wage expenditure commitments, excluding the $78 million in Gaza emergency spending mentioned above, were higher than the pro-rated budget amount by about $58 million. The latter amount includes higher operational expenditures (by $32 million), as well as budget-financed "minor capital expenditures" (by about $41 million), offset in part by lower transfers and subsidies (by $15 million). Operational expenditures reflected lumpy spending in the first half of the year,[7] and are expected to be significantly lower in the remainder of the year. The Ministry of Finance believes that there is scope to restrain operational spending sufficiently to keep non-wage spending within the year's budget ceiling, especially given the high allocation for operational spending in the 2009 budget (about 35 percent higher than was spent in 2008).

- Net lending (including payments by the central government for utility bills owed by municipalities) was in line with the prorated budget projection. Measures to raise utility collection rates continued to be implemented, including better monitoring and incentives for payment of bills by municipalities, as well as installation of prepaid meters.

- Donor aid to finance the recurrent budget in the first half of 2009 has been lower than had been envisaged in the 2009 budget. During January to June 2009 about $406 million was disbursed in donor aid for the recurrent budget, compared to $575 million that the budget anticipated for the first half of the year (excluding Gaza emergency spending). This shortfall, along with higher-than-budgeted non-wage expenditures, notably for Gaza, had led the PA to borrow about $287 million from domestic banks.[8] The shortfall has also contributed to postponement of payments amounting to about $180 million.[9] While it is too early to formally classify the latter as "arrears" before six months have elapsed from the time of commitment, it is likely

[7] The lumpy spending included contracts signed by the Ministry of Health early in 2009 for hospital and pharmaceutical supplies needed during 2009, as well as contracts signed by the Ministry of Education for school and university supplies for the 2009–10 academic year.

[8] In July 2009, the PA repaid about $111 million to commercial banks, thus resulting in net bank borrowing of $176 million during January to July 2009. The total stock of government debt to domestic banks is estimated at about $750 million as of end-June 2009, and about $640 million as of end-July 2009.

[9] The $180 million in delays/possible arrears accumulated in the first half of 2009 includes about $40 million for the payment of employees' wage contribution to the pension fund, and $140 million for the payment of the government's contributions to the pension fund for its public sector employees as well as payments due to private sector suppliers.

that a significant part of it will become arrears by end-2009 unless sufficient donor aid is disbursed to finance the budget gap.

9. **The recurrent fiscal deficit for 2009 is projected to be higher than envisaged in the 2009 budget** (Tables 2a, 2b). The budget, which was prepared before the war, targeted a recurrent deficit of 18.2 percent of GDP for 2009. The recurrent deficit, excluding Gaza emergency recurrent spending, is projected to be higher than budgeted by about $40 million, or at about 18.5 percent of GDP, mostly on account of lower-than-expected clearance revenues due to the war. If the recurrent emergency spending for Gaza of $300 million is included, as envisaged in the budget amendment, the 2009 recurrent deficit is projected at 23.2 percent.

Fiscal Indicators for 2008–10

(In millions of U.S. dollars, unless otherwise indicated)

	2008	2009			2010
		Budget	Jan.-Jun. Est.	Year Proj.	Year Proj.
Total net revenues	1,568	1,630	669	1,588	1,770
Gross domestic revenues	562	625	212	632	698
Gross clearance revenues	1,122	1,123	494	1,074	1,201
Tax refunds	116	118	37	118	129
Total recurrent expenditures (commitment):	2,886	3,080	1,506	3,080	2,988
Wage spending	1,453	1,410	689	1,410	1,466
Non-wage spending	985	990	553	990	1,222
Operational expenditures	293	400	232	357	452
Transfers and subsidies	634	558	264	558	730
Minor capital expenditures	59	32	57	75	40
Net lending	447	380	186	380	300
Gaza emergency spending	0	300	78	300	0
Total recurrent expenditures (cash)	3,273	2,780	1,258	2,780	2,988
Recurrent balance (commitment basis):					
without Gaza emergency spending	-1,317	-1,150	-760	-1,192	-1,218
with Gaza emergency spending	…	-1,450	-838	-1,492	-1,218
Recurrent balance (cash basis)	-1,690	-1,450	-633	-1,492	-1,218
Development projects	191	1,103	63	400	667
Overall balance (cash basis, including capital expenditures)	-1,881	-2,553	-695	-1,892	-1,885
Financing	1,881	2,553	695	1,892	1,885
External support for recurrent and capital expenditures	1,955	2,557	438	1,729	1,889
Domestic financing	-29	0	287	176	0
Net external debt	-4	-4	0	-13	-4
Memorandum items:					
GDP	6,540	6,318	6,442	6,442	7,000
Recurrent balance (commitment basis), percent of GDP:					
without Gaza emergency spending	-20.1	-18.2	-11.8	-18.5	-17.4
with Gaza emergency spending	…	-23.0	-13.0	-23.2	-17.4
Expenditure arrears (US$ millions)	-387	0	180	0	0
Expenditure arrears (in percent of GDP)	-5.9	0.0	2.8	0.0	0.0
Recurrent balance (cash basis), percent of GDP	-25.8	-23.0	-9.8	-23.2	-17.4

Sources: Ministry of Finance; and IMF staff estimates.

10. **There is a need to secure additional donor aid to finance the 2009 recurrent deficit.** From January to end-August 2009, about $0.95 billion in donor aid has been disbursed, which is in line with the amount anticipated given the deficit of $1.15 billion forecast in the original 2009 budget for the year as a whole. However, over half of that amount (about $0.54 billion) was disbursed as late as July and August, contributing to the PA's liquidity difficulties and recourse to bank borrowing in the first half of the year. Net bank borrowing for 2009, as of end-July, is estimated at about $0.2 billion. Given the projected deficit of $1.5 billion, this implies about $0.4 billion in external financing requirements for September to December 2009. It is assumed that expenditure arrears accumulated during 2009 will be repaid in the remainder of the year, and that the stock of commercial bank debt accumulated up to end-July 2009 will be repaid gradually in the longer term.

11. **The PA has continued to strengthen the Public Finance Management System**, which has helped prioritize and raise the quality of public expenditures. The implementation of measures since mid-2007 to increase transparency and accountability has greatly facilitated the disbursement of donor aid directly to the PA budget.[10] Expenditure management was further enhanced in 2009:

- The process of rolling out the new computerized accounting system from the MoF to line ministries was completed in August 2009, with a view to giving line ministries increased ownership for financial management, and improving the quality of budget execution.

- The MoF, with technical assistance from DFID, has made good progress during 2009 in the preparation of FY 2008 financial statements, with the aim of having the audit completed by the State Audit and Administrative Control Bureau (SAAC) by end-2009. The SAAC has received technical assistance from the Norwegian Audit Bureau during 2009 to strengthen its capacity and expedite the completion of the audit.

- To further strengthen commitment controls and cash management, the MoF has received technical assistance from the Fund and the Bank during 2009 to develop a yearly cash plan. Building on this experience, the MoF intends to develop a plan for 2010 that will guide budget execution during the year, with forecasts of monthly

[10] For details on the reform of the pubic finance management system since 2007, see the IMF reports on reviews of progress on www.imf.org/wbg, "Medium-Term Macroeconomic and Fiscal Framework for the West Bank and Gaza", December 2007 to February 2009. The Ministry of Finance's monthly budget execution reports, quarterly reports on fiscal developments and reforms, and a strategy paper entitled "Palestinian Economic Recovery Strategy in Transition," are published on the ministry's website www.pmof.ps.

revenues, expenditures and the deficit. This will help align ministries' spending commitments with available cash, thus helping minimize arrears accumulation.

- To enhance the operation of the MoF's Central Treasury Account (CTA), the process of opening "zero balance" accounts for line ministries was completed in August 2009. In conjunction with this process, bank accounts outside the CTA are being progressively closed.

- A new web-based budget information system was completed in July 2009, which will allow line ministries to present to the MoF more detailed and easier-to-compile spending plans for the preparation of the 2010 budget.

III. Macroeconomic Outlook

12. **The macroeconomic framework assumes that all parties (PA, the GoI, and donors) will proactively push the peace process forward and support growth-enhancing reforms and institution-building**. In particular, it assumes, first, that the trade environment would continue to improve, both within the Palestinian territories and with the rest of the world, which will require a continuation of the process of lifting restrictions on movement and access in the West Bank and of the blockade on Gaza. Second, the PA would continue with a prudent fiscal policy based on expenditure restraint, institution- and capacity-building, and structural reforms (Box 2). Third, donors would provide adequate and timely financial assistance to cover both the recurrent budget deficit and expanded public investment and reconstruction needs.

13. **For 2009, with the above policy expectations, real GDP growth in the WBG is projected to increase to 5½ percent in 2009, from about 2¼ percent in 2008.** Real GDP growth in the West Bank is projected to rise from about 5 percent to 7 percent, while in Gaza there would be an upturn in growth from -5 percent to about 1 percent. This expansion assumes that, in the remainder of 2009, remaining restrictions on movement and access in the West Bank will be lifted, while Gaza's blockade will be eased to allow the entry of reconstruction capital goods and raw materials. While trade with Israel could be affected by the global slowdown,[11] the WBG's growth prospects would be much more strongly influenced by the lifting of restrictions. The above growth rates imply that Gaza's real GDP per capita would continue to decline, in contrast to the West Bank where real GDP per capita would grow by about 4 percent, representing the first significant improvement in living standards since 2005.

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[11] Israel's real GDP growth is projected to decline from about 4¼ percent in 2008 to ½ percent in 2009, due largely to the impact of the global recession on its investments and exports, and to gradually recover to an average of about 4 percent in 2010-12. Israel's inflation is projected to fall from 4¾ percent in 2008 to 1½ percent in 2009 reflecting falling world commodity prices. For more details on the economic outlook for Israel, see the IMF staff reports for Israel's Article IV Consultations published on www.imf.org.

Box 2. Structural Reforms for Fiscal Sustainability

Progress toward fiscal sustainability requires a steady decline in the budget deficit over the medium term, from a projected 18.5 percent of GDP in 2009 to about 11 percent of GDP by 2012, and further reductions thereafter toward a balanced position. To undertake such an adjustment, a prudent overall expenditure stance should be supported by key structural reforms**:**

- **A comprehensive civil service reform**, combining adjustments of salary scales and restructuring, will be needed to ensure a steady decline in the wage bill along with enhanced public sector efficiency. A continuation of the process of lifting restrictions is bound to further raise private sector growth, which would facilitate such a reform, including personnel reductions in the civil service. Public sector efficiency is already being enhanced by the ongoing reform of the security forces.

- The impact of fiscal austerity on the poor needs to be eased by **streamlined and better targeted social transfers**. It is important that the social safety net strategy, currently being developed with World Bank assistance, be finalized as soon as possible so as to allow its prompt implementation in 2010. The strategy has been designed to include an appropriate electricity tariff policy to help protect the poor from the impact of price increases resulting from the commercialization of electricity distribution. The new database on poor households, also developed jointly with the World Bank, should be employed to minimize the degree of overlap and leakage of social transfers to the nonpoor. A better targeted social safety net would make it easier for the PA to steadily reduce the size of the public sector.

- The PA is currently preparing, with World Bank technical assistance, an action plan to **restore the viability of the public pension system**. The plan, which is expected to be finalized by end-2009 and implemented in 2010, includes steps to roll back early retirement provisions, reduce replacement rates, and implement legislation to ensure that financial assets are safeguarded for the benefit of pension plan participants.

- Measures to improve the collection of utility bills should be complemented by a **reform of the electricity sector**. An important step has been the signing by the President in April 2009 of the new Electricity Law, which has paved the way for a World Bank-supported project to fully transfer, by end-2010, electricity distribution from municipal control to utility companies that operate on a commercial basis.

14. **Over the medium term, under the baseline scenario, real GDP growth in the WBG is projected to be in the range of 7 to 8 percent per year.** This assumes that Gaza's blockade continues to be eased to allow unimpeded passage of consumer and investment goods, and that trade restrictions between the West Bank and Israel would be lifted. The WBG's potential for sustained growth has always been heavily reliant on trade with Israel, given the long common border, Israel's much larger economy in both absolute and per capita

terms, as well as the fact that Israel is the WBG's key outlet to external markets in the absence of a functioning domestic seaport or airport.[12]

15. **A rise in donor-funded and private investments consistent with the peace process should offset the impact of fiscal consolidation as well as contribute to longer-run growth.** The share of recurrent public expenditures in GDP would decline by over 7 percentage points over 2009–12 (excluding emergency spending for Gaza), making room for higher public investment while reducing reliance on external financing for budgetary support. As a result of the improved trade environment, exports and imports of goods and services would rise in real terms by a yearly average of 9 to 12 percent over the period 2009–12.

16. **Stepping up structural reforms is key to achieving the baseline scenario targets and a move toward fiscal sustainability**. First, it will be difficult to continue to reduce the wage bill by relying only on containment of the general wage rate and of new employment. A comprehensive civil service reform will be essential to durably reduce the wage bill while raising public sector efficiency. Second, the social safety net strategy should be implemented as soon as possible to contain the rise in social transfers through more efficient targeting of assistance to the truly needy. Third, reform of the public pension system is important to contain the rise in budgetary payments to retirees and prevent further accumulation of arrears to the pension fund. Finally, the projected decline in net lending will be difficult to achieve without reform of the electricity sector to improve the efficiency of utility provision while steadily raising utility bill collection rates.

17. **The 2010 Budget Circular[13] targets a further decline in the recurrent budget deficit (excluding emergency spending on Gaza) from $1.5 billion in 2009 to $1.2 billion in 2010**, based on the following measures:

- Restraint will continue to be exercised on the wage rate and on new employment. The wage bill is envisaged to grow by a maximum of 4 percent in nominal terms, reflecting a ceiling for a general wage rate increase of 2 percent, and a 2 percent increase in employment due to a net addition of 3,000 health and education workers.
- Measures to phase out utility subsidies will continue to be strictly applied. Utility bill collection rates are expected to rise due to continued enforcement of measures to improve compliance, installation of prepaid meters, and the transfer of electricity

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[12] Israel's GDP in 2008 is estimated to be about thirty times as large as that of the WBG, while its GDP per capita is about fifteen times higher. Since the onset of the occupation in 1967, over three-fourths of the WBG's exports and imports of goods and services have gone to, or come from, Israel.

[13] The Circular was prepared by the MoF in August 2009, with a view to submission of the draft budget to the Cabinet by mid-November 2009.

distribution in the West Bank from local governments to utility companies that operate on a commercial basis.

- The implementation of development projects is projected to accelerate in 2010, reflecting the hoped-for facilitation of movement of project personnel, capital goods and raw materials in the West Bank, and the easing of Gaza's blockade. As a result, public investment would rise by over 50 percent to a total of $670 million in 2010.[14]

- The revenue-to-GDP ratio is projected to recover toward more typical past levels, reflecting (i) a significant recovery in real incomes; (ii) improved compliance as a result of the relaxation of restrictions on movement and access and the restoration of law and order in West Bank cities; (iii) recovery from the impact of the Gaza war on clearance revenues; and (iv) continued improvements in tax administration, including the strengthening of the Customs Department.[15]

18. **While the projected recovery would be a major achievement, it would still leave living standards below pre-closures levels in 2000**. Real GDP is estimated to have declined by a cumulative 13 percent since the imposition of restrictions on movement and access in 2000 up to 2008 (or a cumulative 30 percent in per capita terms), suggesting that income in the Palestinian economy is well below potential. Even in this scenario, real income per capita in 2012 would still be about 20 percent below its level in 2000. While the rate of unemployment rate would decline substantially to 13 percent by 2012, it would still be higher than the 12 percent recorded in 1999.

19. **The above projections are subject to the risk that the peace process will be stalled, and that the process of lifting restrictions on movement and access will not continue**. Given that risk, a "pessimistic" scenario was developed according to which Gaza's blockade and restrictions would not be relaxed further, thus inhibiting further expansion in trade and private investment and hindering the implementation of the donor-financed public investment program and reconstruction, with the following implications:

- Slower revenue growth, combined with rising social and emergency spending, would substantially reduce the pace of fiscal consolidation and structural reforms, even with a continued strict policy on government wages and employment. The recurrent budget deficit would decline very slowly, and would be as high as 20 percent of GDP even

[14] The sharp rise in public investment reflects the fact that in 2009, only about $150 million out of the $600 million planned for that year in the PA's Gaza Reconstruction Plan could be implemented due to the persistence of the blockade on investment goods. The assumption in the 2010 budget is that the blockade would be eased to allow a rise in Gaza reconstruction investments to about $450 million, while about $220 million would be spent on other public investments including in the West Bank.

[15] As part of a project funded by the European Union, the Palestinian Customs Department adopted in 2009 a modern web system that will substantially simplify customs procedures and reduce tax evasion.

by 2012 (compared to 11 percent in the baseline scenario). Assuming the same level of external support for the recurrent budget as in the baseline scenario, at an average of about $1.2 billion per year, cash spending would need to be curtailed and significant expenditure arrears would accumulate.

- Continued restrictions on imports of capital goods and raw materials and passage of project personnel would reduce the pace of implementation of public investment and Gaza's reconstruction. This would have an adverse impact on longer-term growth, in addition to its immediate impact on private sector activity.
- With private activity remaining subdued due to continuing restrictions on movement and access, and with public consumption and investment restrained, real GDP per capita is expected be stagnant over the period 2009–12. Unemployment would rise from 26 percent in 2008 to 30 percent by 2012. The risk of social upheaval would also rise as a consequence, which by itself will put further pressure on private sector growth and make it increasingly difficult to restrain public sector wages and employment.

West Bank and Gaza: Comparison with Pessimistic Scenario

	2008 Est.	2009	2010	2011	2012	2009	2010	2011	2012
		Baseline Scenario				Pessimistic Scenario			
Output and Investment									
Real GDP (percentage change)	2.3	5.5	6.5	7.5	7.7	2.7	3.0	3.3	3.5
Real GDP per capita (percentage change)	-0.5	2.6	3.5	4.5	4.7	-0.2	0.1	0.3	0.6
Gross capital formation (in percent of GDP)	18.0	21.7	26.1	25.7	25.7	17.8	19.2	20.0	20.1
Of which: public investment (in percent of GDP)	3.3	6.7	10.0	8.8	7.9	3.5	5.2	6.3	6.4
			(In percent of GDP)						
Public finances 1/									
Revenues 2/	24.0	24.7	25.3	26.1	26.4	23.5	23.5	23.5	23.5
Recurrent expenditures and net lending	44.1	47.8	42.7	40.0	37.5	50.7	45.6	44.7	43.5
Recurrent balance (before external support) 2/	-20.1	-23.2	-17.4	-13.9	-11.1	-27.2	-22.1	-21.3	-20.0
Recurrent balance, cash basis (before external support) 2/	-25.8	-23.2	-17.4	-13.9	-11.1	-23.5	-18.1	-15.1	-12.6
Expenditure arrears accumulation	-5.9	0.0	0.0	0.0	0.0	3.7	4.0	6.1	7.5
Capital expenditures	3.3	6.7	10.0	8.8	7.9	3.5	5.2	6.3	6.4
(In millions of U.S. dollars)	191	400	667	650	650	200	325	425	465
External recurrent budgetary support (in billions of U.S. dollars)	1.8	1.3	1.2	1.1	1.0	1.3	1.2	1.1	1.0
Total external support, including for capital expenditures	29.9	26.8	27.0	22.3	18.7	24.1	23.0	21.1	18.7
(In billions of U.S. dollars)	2.0	1.7	1.9	1.7	1.6	1.5	1.5	1.5	1.4
			(In percent of GDP)						
External sector									
Exports of goods and nonfactor services	13.0	13.1	13.7	15.0	15.6	12.1	11.8	11.8	11.7
Import of goods and nonfactor services	70.2	71.7	75.2	72.8	71.7	68.9	69.2	68.5	67.6
Current account balance (excluding official transfers)	-26.1	-29.4	-29.4	-25.6	-23.8	-27.3	-26.4	-24.8	-23.1
Current account balance (including official transfers)	3.8	-2.6	-2.4	-3.3	-5.1	-3.2	-3.4	-3.7	-4.4
Memorandum items:									
Unemployment rate (average in percent of labor force)	26.0	23.6	20.1	16.8	13.0	25.8	26.7	28.0	29.7

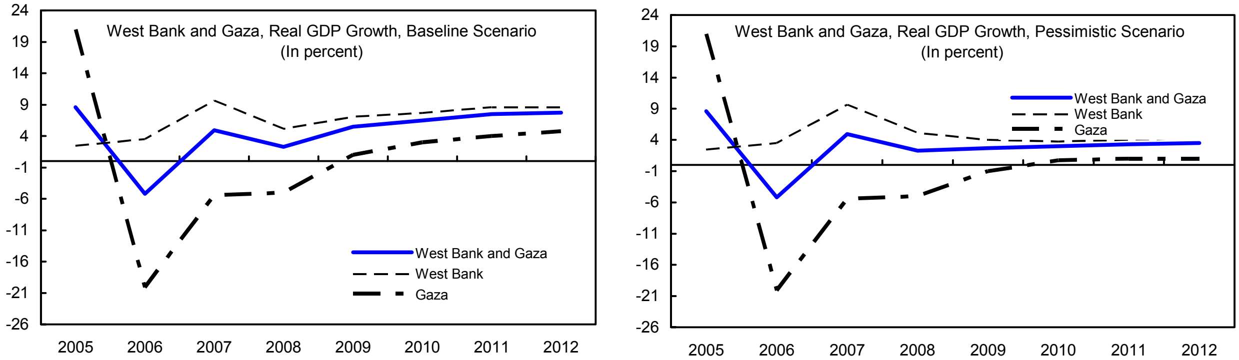
Sources: Palestinian authorities; and IMF staff estimates.

1/ Commitment basis.

2/ For 2008, revenues exclude the special dividend from the Palestinian Investment Fund (PIF) of $197 million.

West Bank and Gaza: Path of Real GDP Growth, 2005–12

Continuation of the blockade and of restrictions on movement and access will adversely affect growth, especially in Gaza.



Sources: Palestinian Central Bureau of Statistics; and IMF staff estimates and projections.

IV. Assessment

20. **IMF staff considers that public finance reforms undertaken so far by the PA, and envisaged to continue in the remainder of 2009 and 2010, are broadly in line with the PRDP.** The PA has maintained discipline to control the growth in the wage bill, and implemented measures to phase out utility subsidies. The Public Finance Management System has been strengthened, which has helped tighten control on expenditures and raise its quality. The institution-building measures and prudent fiscal policy have complemented the positive impact of the easing of restrictions on private sector confidence. The easing of restrictions and higher growth should support an acceleration of structural reforms, including comprehensive civil service and pension system reforms. The PA's commitment to stepping up public finance reforms was reaffirmed in the "Program of the Thirteenth Government" for 2010–11 issued in August 2009.

21. **Given the difficult liquidity situation, it is particularly important for the PA to pursue a sufficiently tight expenditure stance in the remainder of 2009 in line with the budget envelope**. There is substantial uncertainty with regard to the amount of donor aid that will be forthcoming to fill the financing gap for the remainder of 2009. It is also important to minimize arrears accumulation and recourse to further bank borrowing to maintain the confidence of private suppliers and commercial banks. While wages and utility subsidies are projected to be well within budgeted levels, it is important to exercise restraint on non-wage spending in the remainder of the year so as not to exceed the budget target for 2009.

22. **To alleviate Gaza's very difficult humanitarian situation, the implementation of emergency recovery projects needs to be accelerated**. A relaxation of the blockade on capital goods and raw materials is necessary to allow reconstruction. In addition, it is important that the PA closely coordinates with donors and implementing UN agencies and NGOs in Gaza to ensure that emergency aid, including the amount envisaged in the budget amendment, is promptly disbursed and effectively used to allow the projects to proceed as

soon as the blockade is relaxed. Such coordination is especially important given the PA's tight budget constraint and the risk of arrears accumulation.

23. **The start of the process of lifting of restrictions has raised hopes that the downward trend in living standards will be reversed in 2009, paving the way for a prosperous era with increased Palestinian self-reliance.** Given past experiences of disappointed hopes at similar junctures, it is essential that all three parties (the PA, GoI, and donors) cooperate closely to contain significant risks to the economic outlook:

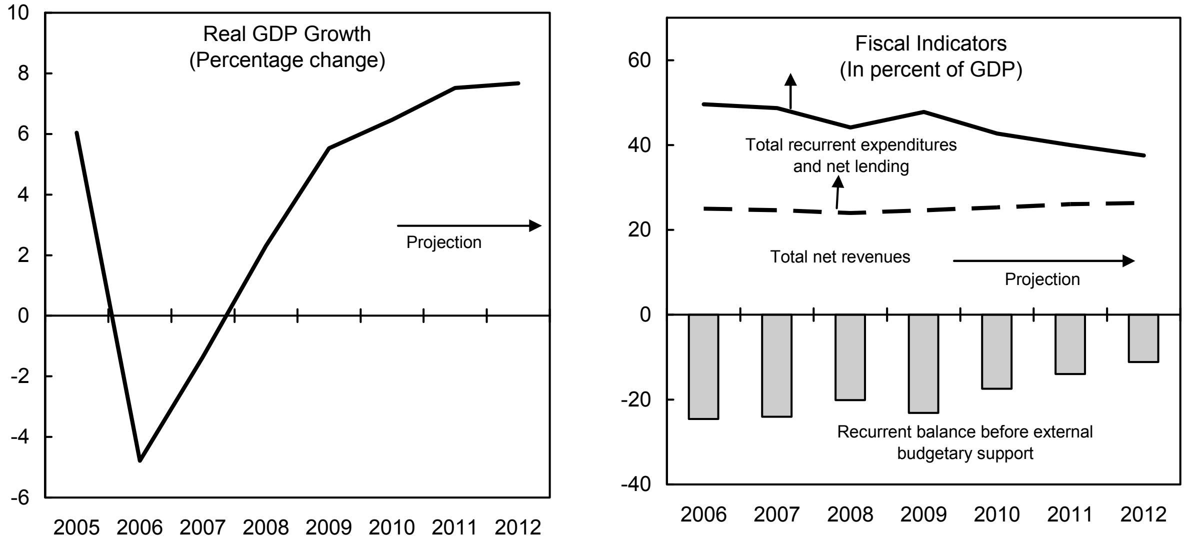
- Further easing of restrictions, and progress in the peace process, are essential for a sustained fiscal retrenchment, private and public investment, and growth in employment and output.

- Donors disbursed a total of $0.95 billion during January to August 2009, in line with the financing requirements of $1.15 billion for the year as a whole forecast in the original 2009 budget. However, over half of that amount (about $0.5 billion) was disbursed as late as in July and August, contributing to liquidity difficulties by the PA and recourse to domestic bank borrowing in the first half of the year. Furthermore, donors were faced with the unexpected challenges from the war in Gaza and its implications for the budget's financing requirements. Additional donor assistance is essential to cover the recurrent budget's external financing needs for September to December 2009 of about $0.4 billion, and of $1.2 billion for 2010. This is in addition to financing needs for development projects projected at $1.1 billion for 2009 and 2010. If adequate funds cannot be secured, the PA would need to cut its cash expenditures and will likely accumulate arrears, including on wages. Close coordination among donors, and between donors and the PA, will be essential to ensure adequate and timely aid disbursements.

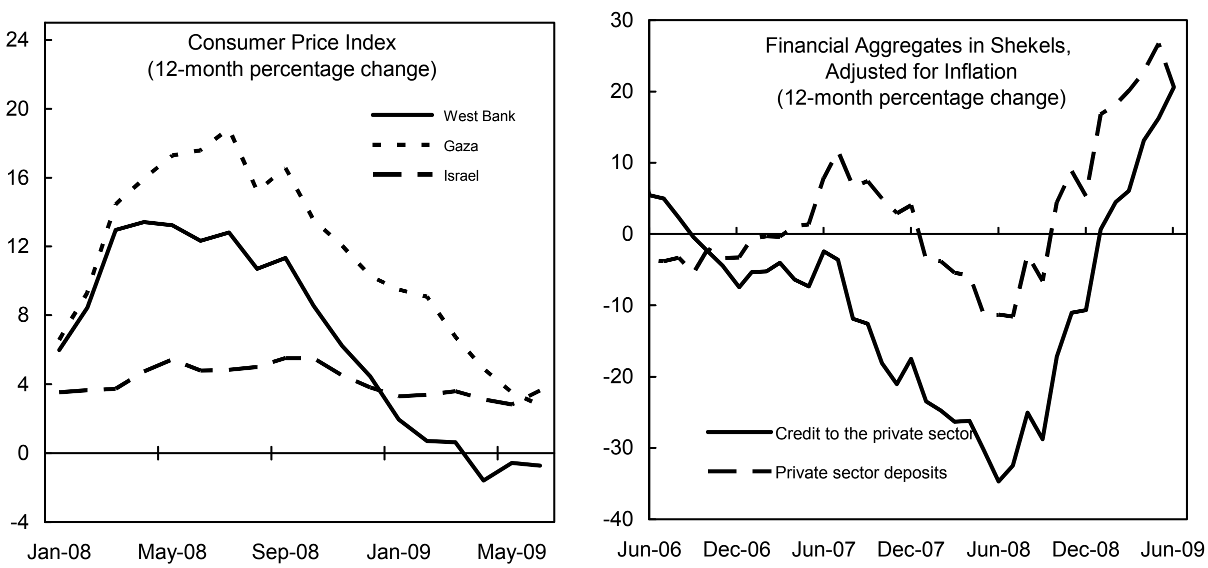
- Given the uncertainties regarding the situation in Gaza, emergency and humanitarian spending needs could turn out to be significantly higher than the amounts currently projected. This would raise the PA's recurrent deficit and require additional donor financing. Furthermore, remaining restrictions on the entry of cash into Gaza need to be lifted to prevent the recurrence of cash shortages. Failure to fully finance the recurrent budget, and to ensure that this financing is translated into cash received by employees and beneficiaries, poses a risk of a further rise in Gaza's poverty rate.

Figure 2. West Bank and Gaza: Macroeconomic and Fiscal Developments

A substantial recovery and fiscal adjustment are envisaged over the medium term, facilitated by a relaxation of restrictions on movement and access.



Inflation has been steadily declining, while real private sector bank credit and deposits have picked up.



Sources: Ministry of Finance; Palestinian Central Bureau of Statistics; and IMF staff estimates.

Table 1. West Bank and Gaza: Selected Economic Indicators, 2006–12
Baseline Scenario

(Population: 3.8 million; 2008 est.)

(Per capita GDP: $1,710; 2008 est.)

(Poverty rate: 57 percent, of which 46 percent in the West Bank and 79 percent in Gaza Strip; 2007 est.)

			Est.	Projections			
	2006	2007	2008	2009	2010	2011	2012
Output and prices	(Annual percentage change)						
Real GDP (2004 market prices)	-4.8	-1.4	2.3	5.5	6.5	7.5	7.7
CPI inflation rate (end-of-period)	3.3	6.9	7.0	3.0	3.0	3.0	3.0
CPI inflation rate (period average)	3.8	2.7	9.9	2.5	3.0	3.0	3.0
Investment and saving	(In percent of GDP)						
Gross capital formation, *of which:*	20.3	17.2	18.0	21.7	26.1	25.7	25.7
Public	5.9	2.3	3.3	6.7	10.0	8.8	7.9
Private	14.5	15.0	14.8	15.0	16.1	16.9	17.8
Gross national savings, *of which:*	12.3	16.4	21.9	19.1	23.8	22.4	20.6
Public 1/	-2.8	-2.5	9.7	3.7	9.6	8.4	7.6
Private	15.1	18.9	12.1	15.4	14.2	14.0	13.0
Saving-investment balance	-8.0	-0.8	3.8	-2.6	-2.4	-3.3	-5.1
Public finances 2/	(In percent of GDP)						
Revenues 3/	25.0	24.7	24.0	24.7	25.3	26.1	26.4
Recurrent expenditures and net lending	49.6	48.7	44.1	47.8	42.7	40.0	37.5
Wage expenditures	26.0	24.9	22.2	21.9	20.9	19.6	18.3
Nonwage expenditures	16.3	13.5	15.1	15.4	17.5	17.3	16.3
Net lending	7.3	10.4	6.8	5.9	4.3	3.2	2.9
Gaza emergency spending	0.0	0.0	0.0	4.7	0.0	0.0	0.0
Recurrent balance (before external support) 3/							
including Gaza emergency spending	-24.6	-24.1	-20.1	-23.2	-17.4	-13.9	-11.1
excluding Gaza emergency spending	-24.6	-24.1	-20.1	-18.5	-17.4	-13.9	-11.1
Recurrent balance, cash basis (before external support) 3/	-15.5	-16.3	-25.8	-23.2	-17.4	-13.9	-11.1
Capital expenditures	5.7	1.9	2.9	6.2	9.5	8.3	7.5
(In millions of U.S. dollars)	260	100	191	400	667	650	650
Overall balance (before external support)	-30.2	-26.0	-23.1	-29.4	-26.9	-22.3	-18.7
External recurrent budgetary support (in billions of U.S. dollars)	0.7	1.0	1.8	1.3	1.2	1.1	1.0
Total external support, including for capital expenditures	21.8	21.6	29.9	26.8	27.0	22.3	18.7
(In billions of U.S. dollars)	1.0	1.1	2.0	1.7	1.9	1.7	1.6
Monetary sector 4/	(Annual percentage change)						
Credit to the private sector	4.1	-5.0	-3.4	13.5	16.4	21.4	21.0
Private sector deposits	8.8	19.8	14.0	8.5	10.7	15.9	15.5
External sector	(In percent of GDP)						
Exports of goods and nonfactor services	11.6	10.4	13.0	13.1	13.7	15.0	15.6
Import of goods and nonfactor services	75.7	68.8	70.2	71.7	75.2	72.8	71.7
Net factor income	11.7	14.4	12.3	11.7	11.7	11.5	11.3
Net current transfers	44.4	43.2	48.8	44.3	47.4	43.0	39.7
Official transfers	21.8	21.6	29.9	26.8	27.0	22.3	18.7
Current account balance (excluding official transfers)	-29.8	-22.4	-26.1	-29.4	-29.4	-25.6	-23.8
Current account balance (including official transfers)	-8.0	-0.8	3.8	-2.6	-2.4	-3.3	-5.1
Memorandum items:							
Nominal GDP (in millions of U.S. dollars)	4,594	5,147	6,540	6,442	7,000	7,800	8,657
Per capita nominal GDP (U.S. dollars)	1,272	1,384	1,710	1,637	1,729	1,872	2,020
Unemployment rate (average in percent of labor force)	23.6	21.5	26.0	23.6	20.1	16.8	13.0
Al Quds stock market index (annual percentage change)	-46.4	-12.8	-16.2	…	…	…	…

Sources: Palestinian authorities; and IMF staff estimates.

1/ The sharp increase in gross public savings during 2008–10 is due mainly to the substantial inflows of donor financing for the recurrent budget and development expenditures.

2/ Commitment basis.

3/ For 2008, revenues exclude the special dividend from the Palestinian Investment Fund (PIF) of $197 million.

4/ End-of-period; in U.S. dollar terms.

Table 2a. West Bank and Gaza: Central Government Fiscal Operations, 2008–12

	Est. 2008	Budget 2009	Projections 2009	2010	2011	2012
	(In millions of U.S. dollars, unless otherwise stated)					
Total net revenues	**1,568**	**1,630**	**1,588**	**1,770**	**2,035**	**2,284**
Gross domestic revenues	562	625	632	698	816	913
Tax revenues	273	273	280	301	342	384
Nontax revenues 1/	289	353	352	396	474	528
Clearance revenues (accrued)	1,122	1,123	1,074	1,201	1,363	1,532
Clearance revenues (cash)	1,137	1,123	1,074	1,201	1,363	1,532
Clearance revenues (net arrears accumulation)	-15	0	0	0	0	0
Tax refunds	116	118	118	129	144	160
Total recurrent expenditures and net lending (commitment basis)	**2,886**	**3,080**	**3,080**	**2,988**	**3,122**	**3,249**
Wage expenditures (commitment)	1,453	1,410	1,410	1,466	1,525	1,586
Wage expenditures (cash)	1,771	1,410	1,410	1,466	1,525	1,586
Wage expenditures (net arrears accumulation)	-317	0	0	0	0	0
Nonwage expenditures (commitment)	985	990	990	1,222	1,347	1,413
Nonwage expenditures (cash)	1,055	990	990	1,222	1,347	1,413
Nonwage expenditures (net arrears accumulation)	-70	0	0	0	0	0
Net lending	447	380	380	300	250	250
Gaza emergency spending	0	300	300	0	0	0
Recurrent balance (commitment basis, before external budgetary support)	**-1,317**	**-1,450**	**-1,492**	**-1,218**	**-1,087**	**-965**
add: expenditure arrears (net accumulation)	-387	0	0	0	0	0
subtract: net clearance withheld (+) or transferred from past collections (-)	-15	0	0	0	0	0
add: arrears on tax refunds	0	0	0	0	0	0
Recurrent balance (cash basis, before external budgetary support)	**-1,690**	**-1,450**	**-1,492**	**-1,218**	**-1,087**	**-965**
Capital expenditures	**191**	**1,103**	**400**	**667**	**650**	**650**
Development projects	191	503	250	217	450	550
Gaza reconstruction related to war	0	600	150	450	200	100
Overall balance (cash basis, including capital expenditures)	**-1,881**	**-2,553**	**-1,892**	**-1,885**	**-1,737**	**-1,615**
Total financing	**1,881**	**2,553**	**1,892**	**1,885**	**1,737**	**1,615**
Net domestic bank financing	-29	0	176	0	0	0
Other domestic financing	0	0	0	0	0	0
External financing for recurrent expenditures (secured)	1,764	0	950	0	0	0
External financing for capital expenditures (secured)	191	0	32	0	0	0
Net external debt	-4	-4	-13	-4	-4	-4
External financing yet to be secured	0	2,557	747	1,889	1,741	1,619
Of which to cover:						
budgetary recurrent expenditure	…	1,454	379	1,222	1,091	969
large projects financed directly by donors	…	32	93	150	250	250
community projects financed directly by donors	…	471	125	200	175	300
Gaza reconstruction related to war	0	600	150	450	200	100
Residual	-40	0	0	0	0	0
Memorandum items:	(In percent of GDP; unless otherwise stated)					
Revenues	24.0	25.8	24.7	25.3	26.1	26.4
Of which: Domestic tax revenues	4.2	4.3	4.3	4.3	4.4	4.4
Of which: Clearance revenues	17.2	17.8	16.7	17.2	17.5	17.7
Recurrent expenditures and net lending	44.1	48.7	47.8	42.7	40.0	37.5
Wage expenditures	22.2	22.3	21.9	20.9	19.6	18.3
Nonwage expenditures	15.1	15.7	15.4	17.5	17.3	16.3
Net lending	6.8	6.0	5.9	4.3	3.2	2.9
Gaza emergency spending	0.0	4.7	4.7	0.0	0.0	0.0
Recurrent balance (commitment basis) before external budgetary support:						
including Gaza emergency spending	-20.1	-23.0	-23.2	-17.4	-13.9	-11.1
excluding Gaza emergency spending	-20.1	-18.2	-18.5	-17.4	-13.9	-11.1
Recurrent balance (cash basis) before external budgetary support	-25.8	-23.0	-23.2	-17.4	-13.9	-11.1
External budgetary support (recurrent)	26.4	23.0	20.6	17.5	14.0	11.2
in millions of U.S. dollars	1,764	1,454	1,329	1,222	1,091	969
Capital expenditures	2.9	17.5	6.2	9.5	8.3	7.5
Overall balance (cash basis)	-28.8	-40.4	-29.4	-26.9	-22.3	-18.7
Total external support (in millions of U.S. dollars)	1,955	2,557	1,729	1,889	1,741	1,619
Nominal GDP (in millions of U.S. dollars)	6,540	6,318	6,442	7,000	7,800	8,657

Sources: Ministry of Finance; and IMF staff estimates.

Table 2b. West Bank and Gaza: Central Government Fiscal Operations, 2008–12

	Est.	Budget	Projections			
	2008	2009	2009	2010	2011	2012
	(In millions of shekels, unless otherwise stated)					
Total net revenues	**5,624**	**6,520**	**6,352**	**7,079**	**8,139**	**9,137**
Gross domestic revenues	2,016	2,500	2,528	2,790	3,264	3,650
Tax revenues	978	1,090	1,120	1,206	1,368	1,538
Nontax revenues 1/	1,037	1,410	1,408	1,585	1,896	2,113
Clearance revenues (accrued)	4,025	4,492	4,296	4,805	5,451	6,129
Clearance revenues (cash)	4,078	4,492	4,296	4,805	5,451	6,129
Clearance revenues (net arrears accumulation)	-52	0	0	0	0	0
Tax refunds	417	472	472	517	576	642
Total recurrent expenditures and net lending (commitment basis)	**10,349**	**12,320**	**12,320**	**11,953**	**12,486**	**12,997**
Wage expenditures (commitment)	5,212	5,640	5,640	5,866	6,100	6,344
Wage expenditures (cash)	6,351	5,640	5,640	5,866	6,100	6,344
Wage expenditures (net arrears accumulation)	-1,139	0	0	0	0	0
Nonwage expenditures (commitment)	3,534	3,960	3,960	4,887	5,386	5,652
Nonwage expenditures (cash)	3,784	3,960	3,960	4,887	5,386	5,652
Nonwage expenditures (net arrears accumulation)	-250	0	0	0	0	0
Net lending	1,603	1,520	1,520	1,200	1,000	1,000
Gaza emergency spending	0	1,200	1,200	0	0	0
Recurrent balance (commitment basis, before external budgetary support)	**-4,725**	**-5,800**	**-5,968**	**-4,874**	**-4,347**	**-3,859**
Add: expenditure arrears (net accumulation)	-1,388	0	0	0	0	0
Subtract: net clearance withheld (+) or transferred from past collections (-)	-52	0	0	0	0	0
add: arrears on tax refunds	0	0	0	0	0	0
Recurrent balance (cash basis, before external budgetary support)	**-6,060**	**-5,800**	**-5,968**	**-4,874**	**-4,347**	**-3,859**
Capital expenditures	**685**	**4,412**	**1,600**	**2,668**	**2,600**	**2,600**
Development projects	685	2,012	1,000	868	1,800	2,200
Gaza reconstruction related to war	0	2,400	600	1,800	800	400
Overall balance (cash basis, including capital expenditures)	**-6,745**	**-10,212**	**-7,568**	**-7,542**	**-6,947**	**-6,459**
Total financing	**6,745**	**10,212**	**7,568**	**7,542**	**6,947**	**6,459**
Net domestic bank financing	-106	0	716	0	0	0
Other domestic financing	0	0	0	0	0	0
External financing for recurrent expenditures (secured)	6,253	0	3,865	0	0	0
External financing for capital expenditures (secured)	685	0	130	0	0	0
Net external debt	-16	-16	-51	-16	-16	-16
External financing yet to be secured	0	10,228	2,908	7,558	6,963	6,475
Of which to cover:						
budgetary recurrent expenditure	…	5,816	1,436	4,890	4,363	3,875
large projects financed directly by donors	…	400	372	600	1,000	1,000
community projects financed directly by donors	…	1,612	500	800	700	1,200
Gaza reconstruction related to war	0	2,400	600	1,800	800	400
Residual	-71	0	0	0	0	0
Memorandum items:	(In percent of GDP; unless otherwise stated)					
Revenues	24.0	25.8	24.7	25.3	26.1	26.4
Of which: Domestic tax revenues	4.2	4.3	4.3	4.3	4.4	4.4
Of which: Clearance revenues	17.2	17.8	16.7	17.2	17.5	17.7
Recurrent expenditures and net lending	44.1	48.8	47.8	42.7	40.0	37.5
Wage expenditures	22.2	22.3	21.9	20.9	19.6	18.3
Nonwage expenditures	15.1	15.7	15.4	17.5	17.3	16.3
Net lending	6.8	6.0	5.9	4.3	3.2	2.9
Gaza emergency spending	0.0	4.7	4.7	0.0	0.0	0.0
Recurrent balance (commitment basis) before external budgetary support:						
including Gaza emergency spending	-20.1	-23.0	-23.2	-17.4	-13.9	-11.1
excluding Gaza emergency spending	-20.1	-18.2	-18.5	-17.4	-13.9	-11.1
Recurrent balance (cash basis) before external budgetary support	-25.8	-23.0	-23.2	-17.4	-13.9	-11.1
External budgetary support (recurrent)	26.4	23.0	20.6	17.5	14.0	11.2
in millions of U.S. dollars	1,764	1,454	1,329	1,222	1,091	969
Capital expenditures	2.9	17.5	6.2	9.5	8.3	7.5
Overall balance (cash basis)	-28.8	-40.4	-29.4	-26.9	-22.3	-18.7
Total external support (in millions of shekels)	6,867	10,228	6,903	7,558	6,963	6,475
Nominal GDP (in millions of shekels)	23,454	25,271	25,767	27,998	31,200	34,628

Sources: Ministry of Finance; and IMF staff estimates.